Supreme Court, U.S.
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No.

IN THE

Supreme Court of the United States

ANTHONY MORELLI,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Can funds that were acquired during a scheme to evade the payment of taxes and that were subsequently wired be "proceeds" of a "specified unlawful activity" for the purposes of the federal money laundering statute, 18 U.S.C. § 1956, even though tax crimes are excluded from the definition of "specified unlawful activity," and even though the subsequent wire transfers of the funds did not generate, produce or yield any "proceeds" other than those the defendant had already acquired by tax evasion?

2. Should this Court resolve a conflict among the circuit courts of appeals on the issue of what constitutes "proceeds" for purposes of the federal money laundering statute?

LIST OF PARTIES

The defendants named in the original indictment were petitioner Anthony Morelli, Joseph Maritato, Edward Dougherty, John Sorrentino, Anthony Zummo, Gregory Federico, Victor Zilber, Mela Rubinov, Arkady Seifer, Igor Roizman, Jacob Dobrer and George Doddy. Thereafter, a superseding indictment was returned naming petitioner, Joseph Maritato, John Brogna, Anthony Zummo, Gregory Federico, Victor Zilber, Mela Rubinov, Arkady Seifer, Igor Roizman, Jacob Dobrer, Vyacheslav Dobrer and George Doddy. Only petitioner, Gregory Federico and Igor Roizman proceeded to trial. After a jury trial, petitioner and his co-defendants were convicted of a variety of crimes, including violations of the Racketeer Influenced and Corrupt Organizations Act ("RICO"), and the federal statutes prohibiting extortion, mail and wire fraud, and money laundering.

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Appendix C — Opinion Of The United States District Court For The District Of New Jersey Dated And Filed February 26, 1996 ..... 59a

Petitioner Anthony Morelli respectfully prays that a writ of certiorari issue to review a judgment of the United States Court of Appeals for the Third Circuit, affirming the calculation of his sentence for violating the RICO statute under the sentencing guidelines for money laundering, even though the "specified unlawful activity" described in the indictment did not generate any "proceeds" that were laundered, and even though petitioner was never convicted of money laundering nor named in any racketeering act alleging money laundering.

OPINIONS BELOW

The Court of Appeals' opinion affirming petitioner's conviction and sentence is reported at 168 F.3d 798 (3d Cir. 1999) (App. A). The opinion of the District Court in *United States v. Morelli*, Crim. No. 93-210 (WGB) (D.N.J. Feb. 26, 1996) is not published, but is reproduced in the appendix (App. C).

STATEMENT OF JURISDICTION

The Court has jurisdiction under 28 U.S.C. § 1254(1). The judgment of the Court of Appeals was entered on March 9, 1999 (App. B).

STATUTORY PROVISIONS INVOLVED

The statutory provision involved in this appeal is 18 U.S.C. § 1956. The subparts of that statute most pertinent to this appeal are:

18 U.S.C. § 1956(a)(1):

> Whoever, knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity, conducts or attempts to conduct such a financial transaction which in fact involves the proceeds of specified unlawful activity — (A)(i) with the intent to promote the carrying on of specified unlawful activity; or . . . (B) knowing that the transaction is designed in whole or in part — (i) to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity . . . [is guilty of money laundering].

18 U.S.C. § 1956(c)(7)(A):

> [T]he term 'specified unlawful activity' means any act or activity constituting an offense listed in section 1961(1) of this title . . . .

Tax fraud is not a "specified unlawful activity" under § 1961(1), and the term "proceeds" is not defined in 18 U.S.C. § 1956.

INTRODUCTION

This case of national importance raises, in sharp focus, issues of statutory interpretation which have bedeviled the federal courts for years.

In this case, the petitioner — a 57 year old man — was sentenced according to the sentencing guideline applicable

to money laundering crimes, even though the indictment did not name him as a defendant in any money laundering count or money laundering racketeering act, and even though the specified unlawful activity described in the indictment did not itself create any proceeds to launder. The result was an increase in the petitioner's sentence from 10 years to 20 years, *i.e.*, a virtual life term.

In affirming the use of the money laundering guidelines to calculate the petitioner's sentence, the Third Circuit's opinion created "proceeds" for the purposes of the money laundering statute where there were none, by interpreting the word "proceeds" expansively, and ignoring the fact that the wiring of funds described in the indictment simply did not result in the petitioner and his co-defendants obtaining any funds beyond those they had previously acquired through their tax fraud scheme. In doing so, the Court of Appeals improperly expanded the meaning of "proceeds" well beyond the meaning intended by Congress when it enacted the money laundering statute, and issued a decision that conflicts with the decisions of other circuits.

In this case, the only scheme that created "proceeds" for Morelli was his tax fraud scheme. If the Court accepts the Third Circuit's reasoning, then any tax fraud scheme in which wire transfers are used to move the proceeds of the tax fraud will become a money laundering case, and tax fraud will have become a "specified unlawful activity" by judicial sleight of hand rather than legislative enactment.

STATEMENT OF THE CASE

A. The Charges Against Morelli

The original indictment charged Morelli in 43 counts, consisting of one count of racketeering conspiracy, one count of racketeering, fourteen counts of extortion, three counts of collection of credit by extortionate means, twelve counts of mail fraud, ten counts of money laundering, one count of conspiracy and one count of conspiracy to commit the crime of money laundering. (R 42).[1] Morelli moved, *inter alia*, to dismiss the money laundering and money laundering conspiracy counts contained in the original indictment. (R 141).

The Government responded by presenting two superseding indictments to the grand jury. (R 159). The second superseding indictment (the "indictment"), on which petitioner was tried, charged Morelli with a variety of crimes. (R 165). The indictment did not charge Morelli with money laundering,[2] nor did it charge him with any racketeering act alleging money laundering. In addition, Morelli was not named in any substantive counts of wire fraud, *i.e.*, the "specified unlawful activity" described in the second superseding indictment's money laundering counts. However, the superseding indictment did charge Morelli with conspiracy, in violation of 18 U.S.C. § 371, and alleged that money laundering was one of three objects

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1. Citations to the Appendix in the Third Circuit are denoted "R __," and the page numbers in such citations refer to the page number of the appendix filed in connection with Morelli's appeal to the Third Circuit.

2. The superseding indictment did, however, charge a number of Morelli's co-defendants with money laundering.

of the conspiracy. The other objects of the conspiracy count were mail and wire fraud. (R 230).

B. The Trial

In this case, the Government proved that Morelli and his co-defendants organized a series of "shell" companies into a "daisy chain," for the purpose of evading the payment of excise taxes on the sale of fuel. During the conspiracy, the companies in the "daisy chain" sold "bootleg" fuel to each other through the chain in a series of paper transactions. After the fuel was sold to the last company in the chain, which was known as the "street company," that company would sell it to a legitimate retailer at a discounted price that was below the "tax-included" market price. The proceeds of the street company's sale would then be sent back through the series of companies in the "daisy chain" by means of a series of wire transfers. (10a).[3]

One of the companies, known as the "burn company," was located in the middle of the "daisy chain." It was legally obligated to collect the excise taxes on the fuel sales and transmit them to the Government. After the proceeds of the fuel sales were wired through the "burn company," however, it would not pay the required excise taxes to the Government, permitting Morelli and his co-conspirators to keep the funds they earned from their sales of fuel to legitimate retailers, without ever collecting the taxes on those sales. (11a).

At trial, the Government did not introduce any evidence to show that Morelli participated in any of the money laundering transactions alleged in the indictment. Indeed,

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3. References to the Appendix are in the form "__a."

the Government did not even offer any proof that Morelli discussed the alleged money laundering transactions with any of his co-conspirators. None of the defendants charged with committing money laundering crimes and racketeering acts relating to money laundering even stood trial with Morelli. Moreover, the Government did not even introduce evidence to show that Morelli participated in the substantive counts of wire fraud that were charged as the "specified unlawful activity" supporting the money laundering counts in the indictment. Thus, there was no evidence that Morelli participated directly in any aspect of the money laundering activity described in the indictment.

Morelli was ultimately convicted of racketeering conspiracy, racketeering, extortion,[4] conspiracy to commit extortion, mail fraud, and the conspiracy count that included money laundering as an object of the conspiracy. (R 351). He was acquitted of a series of mail fraud charges. *Id.* Thus, the sole connection between Morelli and the alleged money laundering described in the indictment was his conviction on a conspiracy count in which money laundering was one of three different objects of the alleged conspiracy, and his conviction on a RICO count that included his co-defendants' money laundering activities as racketeering acts.[5]

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4. The "extortion" Morelli stands convicted of was principally based on the threat of economic harm to the businesses of others, in the form of a "price war" for fuel. At trial, there was no testimony or other evidence indicating that Morelli committed any act of physical violence in furtherance of the "daisy chain" schemes described in the indictment.

5. Curiously, the jury's verdict form found Morelli liable for the racketeering acts that alleged money laundering activity, even

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C. The Sentencing Proceedings

Although Morelli's connection to the money laundering charges in the indictment was extremely attenuated, the District Court followed the recommendation of the Probation Department and applied the money laundering guidelines in calculating Morelli's sentence. The result was a dramatic increase in Morelli's sentencing exposure.

The Probation Department calculated Morelli's sentencing guidelines by separating the charges on which he was convicted into three categories: 1) crimes sounding in extortion; 2) crimes sounding in fraud; and 3) crimes sounding in money laundering. Morelli's base offense level in connection with the extortion crimes was 24. His base offense level in connection with the fraud crimes was 30. His base offense level in connection with the money laundering crimes was 39. (43a).

Because the base offense level associated with the money laundering crimes was so much higher than the level associated with the other groups, Morelli's final base offense

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though Morelli was not named in those acts. In its sentencing opinion, the District Court speculated that Morelli's

> liability for those acts is apparently based on the jury's determination that (i) he had agreed to be a member of the RICO conspiracy; (ii) his coconspirators agreed that money laundering offenses would be committed in furtherance of the conspiracy; and (iii) the commission of the money laundering offenses was foreseeable.

(42a).

level was not increased to account for the crimes associated with his alleged extortions and frauds — *i.e.*, the crimes he was actually convicted of committing. With a base offense level of 39, the Probation Department calculated Morelli's sentencing range as 324-405 months. (43a).

The dramatic impact of the money laundering calculations is starkly demonstrated by re-calculating Morelli's sentence based on the fraud and extortion calculations alone. If the Probation Department had calculated Morelli's sentencing guidelines by grouping his crimes into only two categories relating to fraud and extortion, Morelli's final base offense level would have been 30, and his sentencing range would have been 121-151 months. (43a). Thus, using the money laundering guidelines more than doubled Morelli's sentencing exposure, even though Morelli's connection to the money laundering conduct charged in this case was minimal at best.

Morelli objected to use of the money laundering guidelines, arguing, *inter alia*, that the Government had not proven the money laundering charges at trial because it had not proven that the alleged laundering involved the "proceeds" of a specified unlawful activity. (R 372-73). Morelli also moved for a downward departure, requesting that the District Court sentence him based on the fraud guidelines, since those guidelines more appropriately described conduct on which he was convicted.[6] (R 378).

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6. As Morelli pointed out in the District Court and again on appeal, even though the Government had prosecuted many "daisy chain" conspiracies before this one, this is the *only* such case in which money laundering counts were charged and the *only* such case in which a RICO conspirator's sentencing guidelines were enhanced using the money laundering guidelines. Morelli's research indicates that his case continues to be unique in this regard.

In sentencing Morelli, the District Court observed that

> what it [Morelli's case] comes down to, basically what we're talking about here is tax fraud. That's really what's happening here. The non-payment of taxes that are due, and the elaborate scheme that's created to prevent that . . . .

(R 494). Despite its reservations, the District Court refused to find that the Government had not proven the money laundering charges in the indictment. However, the District Court did conclude that the resulting sentence overstated the seriousness of Morelli's crime, and therefore departed downward a total of three base offense levels when calculating Morelli's money laundering guidelines base offense level. (58a).

After ruling on other sentencing issues, the District Court ultimately found that Morelli's final base offense level was 36, and that, at that level, his sentencing range was 235-293 months. (58a). On this basis, the District Court imposed a sentence of 240 months on Morelli. (62a). Thus, Morelli's ultimate sentence, even after the District Court's downward departure, was almost twice what it would have been if the District Court had employed the fraud guidelines — which were clearly the most applicable to Morelli's actions — to calculate Morelli's sentence.

D. Proceedings In The Third Circuit

1. *Morelli's Argument*

In the Third Circuit, Morelli continued to argue, *inter alia*, that even if the proceeds of the fuel sales described in

the indictment were "proceeds" of a fraudulent scheme, the scheme that generated the "proceeds" was a scheme to avoid the payment of excise taxes. Thus, Morelli argued, no "proceeds" were created by the subsequent wirings of funds that were described in the indictment. (3a). Therefore, the only proceeds in this case were generated by a crime — tax fraud — that was not a "specified unlawful activity" sufficient to serve as a predicate for a money laundering charge. *Id.* In pressing this argument, Morelli noted that a wire fraud may be established without any proof that the wire fraud generated any illicit profit, and emphasized that the Government had argued this point in the District Court. (16a).

2. *The Court Of Appeals' Opinion*

In affirming the judgment of the District Court, the Third Circuit began by acknowledging that, when the "street company" initially sold "bootleg" fuel to a retailer, the "street company" acquired the proceeds of a tax fraud, not a wire fraud (20a). Specifically, the Court noted

> We think it is obvious that the money that the [conspirators] fraudulently obtained [by their initial sale of fuel through the "street company"] does not "result, proceed, or accrue" from this single series of wirings, and therefore the money is not the proceeds of a wire fraud. Within the individual series of transactions, the money is the proceeds of fraud simpliciter at the time it enters the Association's hands [through the "street company"]. The later wirings do not change its character into the proceeds of wire fraud (17a).

The Court of Appeals went on, however, to find that the funds acquired by the "street company" from *subsequent* sales of bootleg, "tax free" fuel *were* the proceeds of a wire fraud scheme, even though Morelli's purpose in establishing the "daisy chains" that sold the fuel was always to evade the payment of excise taxes. In making this ruling, the Court of Appeals *sua sponte* created a theory to support the Government's money laundering allegations that had *never* been described in any of the indictments, and that had *never* been argued by the Government at Morelli's trial, his sentencing, or his appeal. That theory was expressed as follows:

> the money [acquired by Morelli and his codefendants] was the proceeds of the *entire* ongoing fraudulent venture . . . . Although each series [of wire transfers] may have included discrete acts of wire fraud that followed the creation of the proceeds related to that series, the fact is that the entire program, encompassing all of the acts charged in the indictment, constituted one large, ongoing wire fraud scheme. Each wiring in each series furthered the execution of each and every individual act of tax fraud, and helped to create the proceeds involved in each succeeding series of transactions. This is primarily because each wiring, whether it occurred before or after a given act of tax fraud, served to promote and conceal each individual embezzlement of taxes, either *ex ante* or *ex post*. More precisely, each wiring, including those that occurred before a particular transaction, made it more difficult for the government to detect the entire fraudulent scheme or any particular

> fraudulent transaction or series of transactions. In sum, the money gained in each series of transactions (save the initial one) was the proceeds of wire fraud because the money was the proceeds of a [tax] fraud that was furthered by the prior wirings (19-20a).

Thus, in the Third Circuit's view, the proceeds of Morelli's ongoing tax fraud scheme were also, simultaneously, proceeds of an ongoing wire fraud scheme, even though the only real profits or "proceeds" earned by Morelli and his conspirators from the scheme were the profits that resulted from their avoidance of excise taxes, and the only reason the wirings charged in the indictment were wire frauds was that those wirings concealed the proceeds of Morelli's tax fraud and thereby furthered his tax fraud scheme.

In formulating this analysis, the Court analogized Morelli's case to that of the defendant in *Schmuck v. United States*, 489 U.S. 705 (1989) (21a). In that case, this Court held that a mailing made subsequent to the completion of one among a series of frauds may be "essential to the perpetuation of [the entire] scheme" because such mailings can be necessary to prevent the discovery of the scheme and thereby keep it operating smoothly. *Schmuck*, 489 U.S. at 711-12. This Court held that the mailings at issue were a sufficient basis to sustain the defendant's conviction under the federal mail fraud statute. *Id.*

In the Court of Appeals' view, the proceeds that were received by the "street companies" in Morelli's "daisy chains" were all the proceeds of wire frauds *after* the initial tax fraud was committed through the use of a "daisy chain,"

even though each individual sale of bootleg fuel by the "street companies" was a tax fraud, and even though the various wire transfers never created any corpus of funds apart from those that Morelli and the other defendants obtained through their tax frauds. According to the Court, this was so because "[e]ach wiring concealed and promoted each and every fraudulent series of transactions by making the entire scheme less detectable," and the money received by Morelli and his coconspirators through the "street companies" was therefore "an acquisition of funds through wire fraud" at the same time the money was received through sales of fuel that were fraudulent because they permitted Morelli and his coconspirators to evade the payment of excise taxes (23a).

The Third Circuit's opinion is thus one large, wobbly circle, in which the funds obtained by a tax fraud scheme are transformed into the "proceeds" of a wire fraud scheme because the wirings "conceal" and "promote" the tax fraud scheme, and in which the newly transformed "proceeds" of the "wire fraud scheme" are then laundered when they are wired from one shell company to another, so that they can be "concealed" and ultimately used to "promote" new sales of bootleg, tax free fuel. The law will not permit a virtual life sentence to be affirmed on this reasoning, which is opposed to both the bulk of the law in the lower courts and common sense.

REASONS FOR GRANTING THE WRIT

I.

BY SENTENCING PETITIONER FOR MONEY LAUNDERING THAT WAS NOT ALLEGED OR PROVEN TO HAVE BEEN COMMITTED, THE DECISION BELOW EFFECTIVELY AND IMPROPERLY REWRITES THE MONEY LAUNDERING STATUTE.

The language of 18 U.S.C. § 1956 explicitly limits the reach of the federal law prohibiting money laundering to transactions that "involve[ ] the proceeds of [a] specified unlawful activity." "Tax fraud" and "tax evasion" are not "specified unlawful activities" for the purposes of 18 U.S.C. § 1956. "Wire fraud" is such a specified unlawful activity, however.

In this case, the Court of Appeals effectively rewrote the statute to punish petitioner for laundering the "proceeds" of tax fraud. Congress never intended this result, and, if followed, the Court of Appeals' reasoning will harshly increase the sentences of tax evaders far beyond what Congress intended.

The opinion below expands the concept of "proceeds" in 18 U.S.C. § 1956 beyond any ordinary understanding of that term, and thereby expands the reach of the federal money laundering statute beyond its well recognized boundaries as set by Congress and interpreted by the courts. As shown below, there simply were no "proceeds" of a wire fraud according to any common understanding of that word, and because there were no such "proceeds," no money laundering transactions took place.

The term "proceeds" is not defined in 18 U.S.C. § 1956, and there is nothing about the use of that term in the statute to suggest that it should have anything other than its ordinary meaning. It is a "fundamental canon of statutory construction[ ] that, unless otherwise defined, words will be interpreted as taking their ordinary, contemporary, common meaning." *Perrin v. United States*, 444 U.S. 37, 42 (1979); *United States v. Alvarez-Sanchez*, 511 U.S. 350, 357 (1994); *Smith v. United States*, 508 U.S. 223, 228 (1993). Black's Law Dictionary defines "proceeds" as "[t]hat which results, proceeds, or accrues from [a] transaction." Similarly, the Merriam Webster Dictionary defines "proceeds" as "the total amount or the profit arising from a business deal." Thus, the term "proceeds" as it is used in the money laundering statute must refer to a *res* or *corpus* of funds that "accrue," "result" or "arise" from a particular crime.

In this case, the money that was wire transferred through the "daisy chain" of shell companies established by Morelli did not "accrue," "result" or "arise" from the wire transfers themselves.[7] As even the Third Circuit acknowledged, at

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7. In fact, as the Government argued vigorously in the District Court, it is possible to commit wire fraud, as Morelli and his co-defendants did in this case, without deriving any "proceeds" from the fraudulent scheme itself. *See, e.g., United States v. DiNome*, 86 F.3d 277, 283 (2d Cir. 1996) (explaining that mail or wire fraud scheme may be complete without loss by victim of scheme); *United States v. Mittelstaedt*, 31 F.3d 1208, 1216 (2d Cir. 1994), *cert. denied sub nom Johnsen v. United States*, 513 U.S. 1084 (1995). Indeed, when it argued in favor of Morelli's sentence in the District Court, the Government argued that the fact that the wire transfers at issue in Morelli's case tended to conceal Morelli's tax fraud

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least with respect to each series of wirings, "the money [was] the proceeds of fraud simpliciter at the time it enter[ed] the [conspiracy]'s hands. The later wirings [did] not change its character into the proceeds of wire fraud" (17a).

The money received by Morelli and his co-conspirators "accrued," "resulted" and "arose" from their sales of fuel to retailers at prices that were below the typical market price because no excise taxes on the fuel had been collected. The fraud that generated the *res* of funds received by Morelli and his co-conspirators was their fraud on the State of New Jersey and the Federal Government, when they represented (through the "burn company") that they would collect and pay over the excise taxes that were due on the fuel they sold, but failed to do so.

Recognizing that the "proceeds" garnered by Morelli and his co-conspirators did not "result," "proceed" or "accrue" in any ordinary sense from the wirings described in the indictment, the Third Circuit nevertheless determined that the funds wired through the "daisy chain" were "proceeds" of a wire fraud scheme in a more metaphysical sense. According to the Third Circuit, the funds were the "proceeds" of a wire fraud scheme simply because the various wirings alleged in the indictment, considered as a whole, made the detection of the scheme by the authorities less likely, and thereby promoted the underlying tax fraud

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(Cont'd)
was sufficient to sustain the wire fraud charges, even though no additional funds were derived from the wire transfers. The Government argued that "for a charge of wire fraud there doesn't have to be proceeds . . . . you don't have to realize a gain to still be convicted of mail or wire fraud." (R 481-82).

committed by Morelli, although they did not cause the funds to be delivered to Morelli and his co-defendants (20a). Thus, in the Third Circuit's view, the wire transfers facilitated the entire fraudulent scheme by concealing it, and because Morelli's tax fraud was facilitated by the wire transfers, that tax fraud was transformed into a species of wire fraud, even though the wire fraud did not "result" in any "proceeds" as that term is commonly understood. By creating this theory of money laundering, the Court of Appeals effectively extended the reach of the money laundering statute to the proceeds of tax crimes, when those proceeds are later transferred by wire. This expansion of the crime of money laundering was simply not contemplated by Congress when it enacted 18 U.S.C. § 1956. The statute does not include tax evasion as a "specified unlawful activity." And the examples of money laundering activity cited in the committee reports relating to the enactment of 18 U.S.C. § 1956 make clear that Congress intended the statute to punish only activity involving a *res* or *corpus* of funds obtained by a distinct crime that is one of the crimes listed as "specified unlawful activity." *See* S. Rep. No. 433, 99th Cong. 2d Sess. (1986), pp. 11-12 (18 U.S.C. § 1956 not intended to apply to "run of the mill" tax evasion, because ordinary tax evasion does not itself generate "proceeds"); H.R. Rep. No. 855, 99th Cong., 2d Sess., pt. 1 (1986); *see United States v. Johnson*, 971 F.2d 562, 568 (10th Cir. 1992).

Under these circumstances, Morelli's sentencing pursuant to the money laundering guidelines can not stand. The Government did not prove that Morelli — or anyone else — laundered the "proceeds" of a wire fraud. At most, the Government showed that Morelli laundered the "proceeds" of a tax fraud. But tax fraud is not a "specified

unlawful activity" for the purposes of the federal money laundering statute, and laundering the proceeds of tax fraud is not a federal crime. By permitting Morelli's sentence under the money laundering guidelines to stand, the Court of Appeals effectively re-wrote the statute proscribing money laundering, extending the reach of that statute far beyond the limits contemplated by Congress.

II.

THE COURT OF APPEALS' OPINION CONFLICTS WITH THE OPINIONS OF OTHER CIRCUITS REGARDING THE DEFINITIONS OF "PROCEEDS" AND "SPECIFIED UNLAWFUL ACTIVITY" UNDER THE FEDERAL MONEY LAUNDERING STATUTE.

Numerous recent Court of Appeals decisions have stated or implied that a money laundering charge can be sustained only if the "specified unlawful activity" described in the charge itself generates a *res* or *corpus* of "proceeds," which are then "laundered." In addition, many Court of Appeals decisions have stated or implied that the "specified unlawful activity" must be separate and analytically distinct from the money laundering crime for which it serves as a predicate. The Court of Appeals' decision directly conflicts with both these lines of authority. It permits a money laundering charge to stand even where no "proceeds" were derived from a "specified unlawful activity" prior to the laundering charged in the indictment, and even where the "specified unlawful activity" and the money laundering charge are not distinct. The Court should issue the writ Morelli seeks, to resolve the conflict among the Circuit Courts as to what "proceeds" are and how they are created by "specified unlawful activity" for the purposes of the

money laundering statute, and to define the relationship between a "specified unlawful activity" and a corresponding money laundering charge.

In virtually every case decided before this one, including a case decided in the Third Circuit itself, the lower courts have described "proceeds" under the money laundering statute as a *corpus* of funds derived from a "specified unlawful activity," which is then "laundered" in a subsequent financial transaction. For example, in *United States v. Conley*, 37 F.3d 970, 980 (3d Cir. 1994), the Third Circuit held that

> proceeds are derived from an already completed offense, or a completed phase of an ongoing offense [and are then laundered] . . . . money, once collected from [illegal gambling activity that is a "specified unlawful activity"], became "proceeds of specified unlawful activity" . . . . Accordingly, any subsequent financial transaction involving those proceeds that promotes or furthers the illegal gambling business could form the basis of a charge of money laundering.

Similarly, the Fifth Circuit, in *United States v. Allen*, 76 F.3d 1348, 1361 (5th Cir.), *cert. denied*, __ U.S. __, 117 S. Ct. 121 (1996), noted that a "fraudulent scheme produces proceeds at the latest when the scheme succeeds in disgorging the funds from the victim and placing them into the control of the perpetrators . . . ," and that "money *produced* from the defendants' fraud became proceeds" when it was delivered to them (emphasis added). In *United States v. Savage*, 67 F.3d 1432, 1442 (9th Cir. 1995), *cert.*

denied, __ U.S. __, 116 S. Ct. 964 (1996), the Ninth Circuit concluded that " 'proceeds' are funds obtained from prior, separate criminal activity." And in *United States v. Christo*, 129 F.3d 578, 580-81 (11th Cir. 1997), the Eleventh Circuit emphasized that, in the context of an alleged bank fraud, no money laundering could occur until a separate *res* or *corpus* of funds created by the defendant's bank fraud was moved through the banking system. *See also United States v. Mankarious*, 151 F.3d 694, 706 (7th Cir. 1998) (predicate offense must produce proceeds in transactions distinct from money laundering transactions); *United States v. Massey*, 48 F.3d 1560, 1566 (10th Cir.) (where defendants obtained money from victims through mail fraud, and lulling letters in mail fraud scheme preceded wire transfers that were charged as money laundering, mail fraud scheme had produced "proceeds" for the purpose of money laundering statute), *cert. denied sub nom Wilkins v. United States*, 515 U.S. 1167 (1995); *United States v. Edgmon*, 952 F.2d 1206, 1213 (10th Cir. 1991) (Congress targeted "post-crime hiding of . . . illgotten gains" when it enacted proscriptions against money laundering), *cert. denied*, 505 U.S. 1223 (1992).

In the present case, the "wire fraud" described in the indictment and in the opinion below did not produce any *corpus* of funds that were subsequently laundered by Morelli's co-conspirators. As even the lower court acknowledged, the funds obtained by Morelli and his co-conspirators did not derive in any ordinary sense from the wirings charged as wire frauds in the indictment; rather, the funds were obtained, in each instance, from a tax fraud. (17a). Despite this fact, the Court of Appeals went on to find that the proceeds of Morelli's tax fraud scheme were *also, simultaneously* the proceeds of a wire fraud scheme "because the money" obtained by tax fraud "was the

proceeds of a fraud that was furthered by the prior wirings" in the scheme, which "served to promote and conceal each individual embezzlement of taxes" committed by Morelli and his co-defendants. (19-20a). In making this finding, the Court of Appeals' decision conflicts with numerous decisions of other Courts of Appeals, and with one of its own prior decisions.

In addition, in the lower courts, a number of cases have explained that the "specified unlawful activity" that generates a *res* or *corpus* of "proceeds" must do so "in acts distinct from the conduct that constitutes money laundering." *United States v. Mankarious*, *supra*, 151 F.3d at 705. That is, "a money laundering transaction must follow and be separate from any transaction necessary for the predicate offense to generate proceeds." *Mankarious*, 151 F.3d at 706; *and see United States v. Savage*, *supra*, 67 F.3d at 1441 ("[w]e conclude that 'proceeds' are funds obtained from prior, separate criminal activity"); *United States v. Johnson*, *supra*, 971 F.2d at 569 ("the money laundering statute was intended to be a separate crime distinct from the underlying offense that generated the money").

In this case, however, as the Court of Appeals acknowledged, the wirings that were the basis for the wire fraud consisted of all the wirings made in each set of "daisy chain" transactions, and were not, in any real sense, distinct from the money laundering transactions described in the indictment. In explaining its ruling, the court below wrote:

> Each wiring concealed and promoted each and every fraudulent series of transactions by making the entire scheme less detectable. Without the

> wirings to make it appear as if a series of distinct transactions between independent companies had occurred, the taxing authorities would have had a much easier time tracking down the perpetrators of the tax fraud scheme. . . . Since each individual fraudulent series of transactions other than the initial one was preceded by a wiring that promoted it, we think that, within each transaction series, the money was the proceeds of wire fraud at the time it came into the hands of the [conspiracy] in the form of the street company. As soon as one wiring took place, the entire tax fraud scheme became a wire fraud scheme. Since the very first series of transactions involved a wiring of the funds, every fraudulent acquisition of funds thereafter was an acquisition of funds through wire fraud (20a).

Thus, in the present case, there was no distinction between the "specified unlawful activity" described by the Court of Appeals and the money laundering crimes charged in the indictment. There was simply a series of wire transfers, all of which were intended, as part of a single scheme, to conceal the proceeds of Morelli's tax fraud. Each series of wirings that the Court of Appeals characterized as "wire fraud" predicates for subsequent money laundering charges were themselves transactions meant to "conceal" the proceeds of a previous tax fraud, and no "proceeds" other than the proceeds of Morelli's tax fraud were ever created by the wirings.

This Court's intervention is necessary to resolve the conflicts among the circuits and to establish a properly circumscribed definition of "proceeds" in accordance with

the clear intent of Congress, and to establish appropriate distinctions between conduct that is "specified unlawful activity" and conduct that is "money laundering" punishable pursuant to 18 U.S.C. § 1956. By granting the petition in this case, the Court will prevent any recurrence of the situation presented here, where the Government doubled Morelli's sentencing exposure by bootstrapping a tax fraud scheme into a wire fraud scheme, and then bootstrapping a wire fraud scheme into a money laundering scheme.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT DATED AND FILED MARCH 9, 1999

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

NOS. 96-5144 and 96-5389

UNITED STATES OF AMERICA

v.

MORELLI, ANTHONY
(D.C. Crim. No. 93-cr-00210-1)
Appellant in No. 96-5144

(Amended per Clerk's order of 7/8/98)

UNITED STATES OF AMERICA

v.

IGOR ROIZMAN, a/k/a Little Igor
(D.C. Crim. No. 93-cr-00210-10)
IGOR ROIZMAN, Appellant in No. 96-5389

On Appeal From the United States District Court
For the District of New Jersey
District Judge: Honorable William G. Bassler

Argued: June 5, 1997
Reargued: September 8, 1998

Appendix A

Before: BECKER, *Chief Judge*, SCIRICA, *Circuit Judge*, and KELLY, *District Judge*.*

(Filed March 9, 1999)

* * *

OPINION OF THE COURT

BECKER, *Chief Judge*.

These appeals by defendants Anthony Morelli and Igor Roizman from judgments in a criminal case raise two issues of criminal law and procedure. Morelli's appeal centers on the interpretation of the federal money laundering statute, 18 U.S.C. § 1956, in the context of wire fraud. Roizman's appeal involves the question of ineffective assistance of counsel where the defendant's attorney faces a possible conflict of interest.

The scheme in which Morelli and Roizman were involved engaged in a series of transactions that resulted in the embezzlement of excise taxes from fuel sales. Each series included a number of wire transfers, each of which occurred after the money involved came into the possession of those who controlled the scheme. At trial, the government proved only that specific transfers had occurred before the point at which the taxes should have been collected for transmittal to the government. Morelli argues that these series of transactions did not constitute money laundering.

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* Honorable James McGirr Kelly, United States District Judge for the Eastern District of Pennsylvania, sitting by designation.

He claims initially that the government failed to prove that any of the transactions involved proceeds of fraud, since the government offered no proof of wire transfers occurring after the point at which the taxes should have been collected. He contends that the money did not become the proceeds of fraud until after it should have been collected for the government but was not. We reject this conclusion because we believe that the money became the proceeds of fraud as soon as it entered the hands of members of the scheme. Alternatively, Morelli submits that the money was not the proceeds of wire fraud because the money came into the possession of the scheme as a result of fraud before any of the wirings involving the money occurred. But he ignores the fact that the scheme succeeded as a result of each and every wiring within each and every series of transactions. Accordingly, the money within each series of transactions was the proceeds of wire fraud because the fraud from which it resulted was promoted by the wire transfers within the preceding series of transactions.

Morelli also contends that the District Court erred in not granting him a downward departure from the money laundering guideline, U.S.S.G. § 2S1.1, because his conduct did not fall within the "heartland" of money laundering. We disagree, and dispose of this contention summarily in note 13 *infra*.

Roizman's appeal alleges that his attorney provided inadequate assistance because of a conflict of interest. Roizman's attorney represented both him and an individual whose statements were introduced at trial as hearsay evidence against him. Roizman first argues that his lawyer's

conduct was deficient since he faced an actual conflict of interest to the extent that his ability to impeach the witness's hearsay statements conflicted with his duties to the witness as his client. The District Court rejected this claim because it found that impeachment of the witness was not a "plausible alternative defense strategy" for Roizman. Because we agree with the District Court's conclusion, and because such impeachment would not have adversely affected the witness's interests, we reject Roizman's argument.

Roizman also contends that his conviction should be reversed on a potential conflict-of-interest theory. He claims that the prosecutor, as well as his own attorney, knew of the conflict his attorney faced and, thus, violated his constitutional rights by not bringing it to the attention of the District Court. We can only grant a reversal for a potential conflict of interest, however, if the District Court itself was or should have been aware of the conflict and failed to address it. Since Roizman does not contend that the District Court should have been aware of the conflict, we reject his claim. We will therefore affirm the judgments of the District Court.

I. Procedural History

Morelli, Roizman and a number of coconspirators participated in a "daisy chain" scheme to evade excise taxes on the sale of certain kinds of fuel. The elements of such schemes have been detailed sufficiently elsewhere. *See, e.g., United States v. Sertich*, 95 F.3d 520, 522 (7th Cir. 1996), *cert. denied*, 519 U.S. 1113 (1997); *United States v. Veksler*,

62 F.3d 544, 547 (3d Cir. 1995); *United States v. Macchia*, 35 F.3d 662, 665-66 (2d Cir. 1994); *United States v. Victoria-21*, 3 F.3d 571, 573 (2d Cir. 1993); *In re Assets of Martin*, 1 F.3d 1351, 1353 (3d Cir. 1993); *United States v. Tarricone*, 996 F.2d 1414, 1416-17 (2d Cir. 1993); *United States v. Aracri*, 968 F.2d 1512, 1514-17 (2d Cir. 1992); *United States v. Musacchia*, 900 F.2d 493, 495-96 (2d Cir. 1990), *vacated*, 955 F.2d 3 (2d Cir. 1991). We will set forth any relevant facts in our discussion of particular substantive issues.

As a result of their activities, Morelli and Roizman were charged in a forty four-count indictment, tried, and convicted of some of the counts. Several other coconspirators pleaded guilty at different times. Morelli was convicted of a RICO conspiracy, racketeering, an extortion conspiracy, extortion, mail fraud, and general conspiracy. With respect to the RICO conspiracy, the jury found that the government had proven money laundering as one of many predicate acts. With respect to the general conspiracy conviction, the jury found that one of the objects of the conspiracy, among others, was money laundering. Morelli was not named in any of the racketeering acts alleging money laundering. However, he was sentenced under the money laundering guideline, which provided the highest offense level. He received a three-point enhancement because he acted as a manager or supervisor of the money laundering conspiracy. The District Court then departed downward three levels, finding that the value of the funds laundered detailed in the Presentence Investigation Report overrepresented the crime. Morelli was sentenced to 240 months in prison. Roizman was convicted of RICO

conspiracy, mail fraud, and extortion, and was sentenced to 90 months in prison. These timely appeals followed.[1]

In addition to the arguments outlined in the introduction, the defendants each make a number of arguments that are patently without merit; hence we identify them and dispose of them summarily in the margin. Morelli contends that the District Court erred in applying his Role in the Offense adjustment to all of his offense groupings for sentencing purposes.[2] He also claims that he should not have been convicted of RICO conspiracy because he did not commit or agree to commit two predicate acts.[3] Finally, Morelli insists that his Sixth Amendment right to counsel was violated because two cooperating witnesses, Dougherty and Zummo, had previously participated in a joint defense

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1. The District Court properly exercised jurisdiction over the matter under 18 U.S.C. § 3231. We exercise appellate jurisdiction over the final judgment of the District Court under 18 U.S.C. § 3742 and 28 U.S.C. § 1291.

2. Morelli submits that the Sentencing Guideline § 3B1.1 enhancement for "Role in the Offense" should have been applied only to the extortion group of crimes, and not the money laundering or fraud groups. The District Court concluded otherwise, and we see no error in its conclusion. The evidence supports the conclusion that Morelli was a "supervisor or manager" with respect to the fraud and money laundering, as well as the extortion.

3. Morelli's appeal on this point rested on his argument that we should reverse our decision in *United States v. Adams*, 759 F.2d 1099 (3d Cir. 1985). However, the Supreme Court has held that our conclusion in *Adams* was correct. *See Salinas v. United States*, 522 U.S. 52 (1997).

agreement.[4] Roizman adopts by reference those of Morelli's claims that are relevant to him.[5]

Following the initial oral argument in this case in June of 1997, we placed it in abeyance pending the Supreme Court's decision in *Salinas v. United States*, 522 U.S. 52 (1997). *See supra* note 3; *see also United States v. Morelli*, Order, Nos. 96-5144 & 96-5389 (3d Cir. June 23, 1997). In the meantime, we remanded certain issues to the District Court for further factual findings. The Supreme Court has now decided *Salinas*, *see supra* note 3, and the District Court has certified its findings on the issues to which we directed its attention, *see supra* note 4 & *infra* Part III. Accordingly, the appeal is now ripe for decision.

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4. The District Court found no such violation of Morelli's Sixth Amendment rights. *United States v. Morelli*, Opinion & Order, Crim. No. 93-210 (D.N.J. Jan. 26, 1998). It concluded that "[t]here was no evidence that either Dougherty or Zummo revealed any confidential defense strategy or any other prejudicial information to the Government." Slip op. at 7. We see no clear error in its finding, and accordingly affirm its conclusion that Morelli's Sixth Amendment rights were not violated. Morelli also argued that the government should have been directed to produce its notes of its meetings with Dougherty and Zummo for Morelli's inspection. Based on our *in camera* inspection of these notes we agree with the District Court that they contained no information pertinent to his claim.

5. Since we affirm the District Court's conclusions on all points, we need not determine precisely which of Morelli's arguments Roizman adopts.

Appendix A

II. Morelli's Appeal

A. Preservation of Issue for Review

We first take up Morelli's argument that the District Court erred in calculating his sentence based primarily on the money laundering guideline, U.S.S.G. § 2S1.1. He contends that, as a matter of law, the facts do not support the conclusion that money laundering occurred. Although Morelli frames this submission as a challenge to his sentence, it is in actuality a sufficiency of the evidence argument. Morelli did not raise this in a Rule 29 motion, which would ordinarily be required of a sufficiency claim. *See United States v. Powell*, 113 F.3d 464, 466-67 (3d Cir. 1997) ("If a defendant fails to file a timely motion for judgment of acquittal, we review sufficiency of evidence for plain error." (citing *United States v. Gaydos*, 108 F.3d 505, 509 (3d Cir.1997))), *cert. denied*, 118 S. Ct. 454 (1997). Nevertheless we find that it is properly before us on the conventional direct appeal standard of review because of the unusual procedural posture, i.e., that this issue is only relevant for sentencing purposes.

Morelli was convicted of a multiple-object general conspiracy and a RICO conspiracy with numerous predicate acts. The jury found that these conspiracies had objects or predicate acts other than money laundering that Morelli does not challenge on appeal. Thus, even if he presented a successful challenge to the money laundering allegations, we would not reverse Morelli's conviction on the conspiracy count because, as he concedes, he was involved in a criminal conspiracy, albeit one to commit mail and wire fraud and

extortion. *See Griffin v. United States*, 502 U.S. 46 (1991); *United States v. Conley (Conley II)*, 92 F.3d 157, 163 (3d Cir. 1996) ("It is clear that when a jury returns a general verdict of guilty on a multi-object conspiracy count, the conviction will stand over Fifth Amendment due process objections so long as there is sufficient evidence to support any one of the objects of the conspiracy."), *cert. denied*, 520 U.S. 1115 (1997). Likewise, he cannot challenge his RICO conspiracy conviction, as he concedes numerous predicate acts, including those same crimes, which are sufficient to support the conviction. *See United States v. Vastola*, 989 F.2d 1318, 1330 (3d Cir. 1993) (applying the reasoning of *Griffin* and concluding that the dismissal of one predicate act did not require reversal of a racketeering conviction where a sufficient number of other predicate acts on which the jury's verdict could have rested remained).

Furthermore, determining the objects of a conspiracy and the predicate acts of a RICO conspiracy for sentencing purposes is the duty of the trial judge, not the jury. *See Conley II*, 92 F.3d at 169 ("[T]he district court's determination of the object of the conspiracy is wholly independent of the jury's determination of the object of the conspiracy."). Since this decision on the part of the District Court is not bound up with the jury's verdict, it need not be challenged in a Rule 29 motion for acquittal notwithstanding the jury's verdict.[6] Rather, a defendant need only challenge

6. Unlike the verdict in *Conley II*, the jury in this case returned a special verdict concerning the objects of the conspiracy and the predicate acts of the RICO conspiracy. Accordingly, the District Court's conclusion that money laundering occurred is buttressed by the jury's special verdicts to similar effect.

the district court's findings as to the objects of the conspiracy and the RICO predicate acts at sentencing in order to preserve the issue for review. Because Morelli raised his present claim in his sentencing hearing, we conclude that it is appropriately before us. "When [as here] the essential facts are not in dispute, our review of the district court's interpretation of the Guidelines, like our review of a statute's interpretation, is plenary." *United States v. Bogusz*, 43 F.3d 82, 85 (3d Cir. 1994) (citing *United States v. Rosen*, 896 F.2d 789, 790-91 (3d Cir.1990)).

B. Money Laundering — Facts and Legal Background

Because the facts of this case are somewhat complicated, we will briefly review those revolving around the alleged money laundering. The particular scheme in which the defendants participated was termed "the Association." The Association organized a group of companies, all of which it controlled, into a "daisy chain," for the purpose of embezzling the excise taxes on the sale of certain kinds of fuel. Typically, the companies would sell oil down the chain in a series of paper transactions, through what was referred to as the "burn company." Eventually, the company at the bottom of the chain, the "street company," would sell the oil to a legitimate retailer, i.e., a particular gas station, for a price slightly below the tax-included market price. This retailer would pay money to the street company, which would send money back up the chain in a series of wire transfers.[7]

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7. The money was not always wired back up the chain via each individual company. Occasionally, a wire transfer would skip

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This scheme was illegal because it was set up as a means to avoid excise taxes. The daisy chain was established so that the burn company was the one legally responsible for collecting the excise taxes on the fuel sales and transmitting them to the government. In the Association's scheme, the burn company would collect the taxes for a time, and then disappear without ever paying the taxes to the government. As a result, the Association could keep the money representing the excise taxes without the government being able to determine where it had gone. The indictment charged, and the jury found, that this conduct constituted both wire fraud and money laundering. It charged the first wire transfer, from the street company to the next company above it in the chain, as wire fraud. It charged the second and subsequent wire transfers as money laundering.

The money laundering statute, 18 U.S.C. § 1956(a)(1), provides:

> Whoever, knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity, conducts or attempts to conduct such a financial transaction which *in fact involves the proceeds of specified unlawful activity* — (A)(i) with the intent to promote the carrying on of specified unlawful

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some companies. In addition, the wire transfers apparently almost always skipped the burn company. As the discussion below demonstrates, however, these details need not concern us, because it is sufficient that the money was wired at least once.

> activity; or . . . (B) knowing that the transaction is designed in whole or in part — (i) to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity . . . [is guilty of money laundering].

The statute, in pertinent part, sets forth four elements of the crime: (1) an actual or attempted financial transaction (2) involving the proceeds of specified unlawful activity; (3) knowledge that the transaction involves the proceeds of some unlawful activity; and (4) either (a) an intent to promote the carrying on of specified unlawful activity, or (b) knowledge that the transaction is designed to promote the underlying specified unlawful activity or "to conceal or disguise the nature [or] the source . . . of the proceeds of specified unlawful activity." 18 U.S.C. § 1956(a)(1). Morelli does not contest the first and third elements. He also does not contest the intent element of money laundering.[8]

The term "specified unlawful activity" is defined, in pertinent part, by reference to those acts that constitute "racketeering acts" under RICO. *See* 18 U.S.C.

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8. He does complain, however, that it is unfair for the government to charge both promotion and concealment with respect to the same transactions. *See United States v. Paramo*, 998 F.2d 1212, 1218 (3d Cir. 1993) (noting that another court has observed that "conduct punishable [as concealment] typically would not also be punishable [as promotion, and vice versa]"). We have noted, however, that these two motivations are not necessarily inconsistent, as "a finding of guilt [for concealment] is not a defense to a prosecution [for promotion]." 998 F.2d at 1218 n.3.

§ 1956(c)(7)(A) ("[T]he term 'specified unlawful activity' means any act or activity constituting an offense listed in section 1961(1) of this title. . . ."). Under § 1961(1), wire fraud is a "specified unlawful activity," but tax fraud simpliciter is not. *See* 18 U.S.C. § 1961(1)(B).

We have interpreted the money laundering statute several times. *See, e.g., United States v. Conley (Conley I)*, 37 F.3d 970 (3d Cir. 1994); *United States v. Paramo*, 998 F.2d 1212 (3d Cir. 1993). *Paramo* focused solely on the fourth element of the statute — whether the defendant's actions constituted sufficient evidence of the appropriate intent. *See* 998 F.2d at 1216-18. In *Conley I*, we focused both on this intent element and on the second element — whether the funds at issue were the "proceeds of a specified unlawful activity." 37 F.3d at 977-81. Whether certain money constitutes "proceeds of specified unlawful activity" is the sole contested question presented in this case.

In *Conley I*, we held that "[a]lthough the money laundering statute does not define when money becomes 'proceeds,' it is obvious to us that proceeds are derived from an already completed offense, or a completed phase of an ongoing offense. . . ." 37 F.3d at 980. This is true even if the money laundering transaction can also be considered a part of the continuing specified unlawful activity. In *Conley I*, the defendant was charged with conspiracy to conduct an illegal gambling business and to commit money laundering. The conspiracy revolved around the distribution and use of illegal video poker machines. The money laundering aspect of the scheme derived from the retrieval and distribution of the money deposited in the machines. We concluded that,

since the distribution and use of the machines alone constituted an illegal gambling business, the specified unlawful activity had been completed at the time the conspiracy's activities resulted in proceeds. Accordingly, the money retrieved from the machines was proceeds of the illegal gambling business, even though the retrieval of the money was also chargeable as part of the crime of conducting the business. *See* 37 F.3d at 980.

This case forces us to decide the question we partially (and tangentially) addressed in *Conley I:* whether the funds involved in the alleged money laundering transaction were "proceeds of specified unlawful activity." Morelli makes two arguments. First, he contends that the money did not become proceeds until after it passed through the burn company. He alleges that this is significant because the government offered no evidence as to how much money was wired after it passed through the burn company, thus failing to prove that money laundering occurred. In the alternative, he claims that, if the money became proceeds before it passed through the burn company, it did so as soon as it came into the Association's control. Thus, it cannot have been the proceeds of wire fraud, since the wire fraud was predicated on the money being wired *after* it entered the control of the Association. We address these points in turn.

C. Did the Transactions Involve the Proceeds of the Fraud?

The government only proved financial transactions, i.e., wirings of money up the daisy chain, occurring before the

money reached the burn company. Accordingly, if the money did not become proceeds until after it passed through the burn company, as Morelli contends, the government's proof of money laundering would have failed because it would not have proved a financial transaction involving proceeds.

Morelli argues that the money did not become proceeds until it moved past the burn company. In essence, he contends that since the duty to pay the taxes lay with the burn company, no fraud occurred until the burn company itself failed to collect and pay the taxes. Hence, before the burn company failed to do so, the money was entirely legitimate. But the taxes were not, as Morelli claims, collected and passed on, and then diverted. They were never collected. The paperwork that indicated that the taxes had been collected was falsified. The transactions going down the chain — purporting to represent sales of fuel — were fraudulent, and the payments going back up the chain were proceeds of that fraud.

In our view, the key point is that the entire chain of companies was operated by the Association; it was all part of the conspiracy. Once the money entered the control of the street company, it entered the control of the Association. The Association never had any intention of paying the taxes. It organized the chain precisely to avoid having to do so. Although in a paperwork sense the taxes were not embezzled until they passed the burn company, the reality is that the taxes were embezzled as soon as the funds entered the chain. The fact that the Association organized the daisy chain to make it appear that distinct companies were buying and

selling the gas and that the tax was collected at each step prior to the burn company does not alter our conclusion. We conclude that the fraud was completed when the money entered the control of the Association acting through the street company, since at that time it had no present intent to pay the taxes. Under these circumstances, the taxing authorities were defrauded out of their funds at the time the money entered the chain.

In sum, we find no reason to set aside the judge's and jury's implicit conclusion that the money derived from this scheme became proceeds for the Association as soon as it entered the street company's hands. Legally, the money was the proceeds of fraud as soon as it entered the hands of the street company.

D. Was the Money the Proceeds of Wire Fraud?

We also think that the money was the proceeds of wire fraud, and not simply tax fraud, which is not a specified RICO predicate act and therefore not a specified unlawful activity under § 1956. Morelli contends that, even if the money became proceeds of some illegal activity at the time it came into the possession of the street company, it was only the proceeds of tax fraud. He argues that, at the time the money entered the hands of the street company, no wire fraud had occurred. Before it was wired, he says, the money was the proceeds of tax fraud. After it was wired, the argument continues, although a wire fraud may have been committed, the money was not the proceeds of a wire fraud, because the wiring itself had nothing to do with the Association's coming into possession of the money.

As an initial matter, we think that Morelli would be correct that the the money would not be the proceeds of wire fraud if only one of these daisy chain series of transactions had occurred. Proceeds are "[t]hat which results, proceeds, or accrues from some possession or transaction." *Black's Law Dictionary* 1204 (6th ed. 1990). The transaction series in question here is the single series of wirings of the funds from the street company up the chain through the burn company to the top. We think it is obvious that the money that the Association fraudulently obtained does not "result, proceed, or accrue" from this single series of wirings, and therefore the money is not the proceeds of wire fraud. Within the individual series of transactions, the money is the proceeds of fraud simpliciter at the time it enters the Association's hands. The later wirings do not change its character into the proceeds of wire fraud.[9]

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9. Accordingly, we disagree with the opinion of the Seventh Circuit in *United States v. Mankarious*, 151 F.3d 694 (7th Cir.), *cert. denied*, 119 S. Ct. 621 (1998). That court, relying on *inter alia Schmuck v. United States*, 489 U.S. 705 (1989), concluded that, unlike bank and wire fraud, "[a] mail fraud scheme . . . can create proceeds long before the mailing ever takes place." 151 F.3d at 705. We think that that court misreads *Schmuck*. In *Schmuck*, the defendant created an ongoing fraudulent scheme that involved a group of independent series of fraudulent transactions. Each of these series ended with a mailing, which the Supreme Court held could provide a basis for mail fraud convictions. The Seventh Circuit apparently reads *Schmuck* as meaning that the mailings rendered the individual series of transactions with which they were associated mail fraud *nunc pro tunc*.

We disagree. As discussed in more detail below, the key in *Schmuck* was not that the mailings increased the likelihood of

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success of the individual fraudulent series of transactions. Rather, each individual mailing contributed to the *future* success of the entire scheme. *See* 489 U.S. at 711-12 (although the mailings may not have contributed to the success of the individual already-completed series of transactions, they were "essential to the perpetuation of Schmuck's scheme"). Thus, we think that *Schmuck* does not support the Seventh Circuit's understanding of the term "proceeds" in the money laundering statute.

We also note that the court in *Mankarious* drew a false distinction between wire and mail fraud. *See Mankarious*, 151 F.3d at 705. As we have noted, the wire fraud and mail fraud statutes differ only in form, not in substance, and cases such as *Schmuck* interpreting one govern the other as well. *See United States v. Frey*, 42 F.3d 795, 797 & n.2 (3d Cir. 1994) (citing *United States v. Tarnopol*, 561 F.2d 466, 475 (3d Cir. 1977) ("[T]he cases interpreting the mail fraud statute are applicable to the wire fraud statute as well.")). Thus, the Seventh Circuit's conclusion would — if correct — apply equally to cases involving wire fraud.

Finally, we observe that none of this implies that Morelli did not conspire to commit wire fraud. A wiring could constitute wire fraud even though it involved money that had already been obtained as a result of fraud. *See United States v. Allen*, 76 F.3d 1348, 1362 (5th Cir. 1996) (holding that "acts occurring after the defrauding defendant already controls the proceeds of the fraud may . . . further the fraud" and accordingly constitute wire fraud); *cf. Schmuck*, 489 U.S. at 712 (holding that mail fraud occurs so long as the mailing is "incident to an essential part of the scheme" (internal quotations omitted)). Clearly, the wirings in this case were "incident to an essential part of the scheme," the transmittal of the money in a useable form to the members of the Association.

This does not get Morelli off the hook, however. We believe that the money wired up from the street company was, in fact, the proceeds of wire fraud, just not in the way Morelli thinks it might have been. In order to understand this, we must engage in a close reading of the wire fraud statute, which reads as follows:

> Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, transmits or causes to be transmitted by means of wire, radio, or television communication in interstate or foreign commerce, any writings, signs, signals, pictures, or sounds for the purpose of executing such scheme or artifice, shall be fined under this title or imprisoned for not more than five years, or both.

18 U.S.C. § 1343. Wire fraud consists of (1) a scheme to defraud and (2) a use of a wire transmission for the purpose of executing, or attempting to execute, the scheme. *See Frey*, 42 F.3d at 797. Morelli concedes that the daisy chain was a scheme to defraud. Furthermore, as discussed above, the scheme produced proceeds. The question is, was the scheme a wire fraud scheme in such a way that its proceeds were the proceeds of wire fraud at the time the Association conducted a financial transaction involving them?

We think the money was the proceeds of the *entire* ongoing fraudulent venture in which the Association

engaged in creating the daisy chain scheme, and that this venture was a wire fraud scheme. This ongoing venture consisted of all the individual series of transactions upon which Morelli focuses, not the discrete series of transactions individually. Although each series may have included discrete acts of wire fraud that followed the creation of the proceeds related to that series, the fact is that the entire program, encompassing all of the acts charged in the indictment, constituted one large, ongoing wire fraud scheme. Each wiring in each series furthered the execution of each and every individual act of tax fraud, and helped to create the proceeds involved in each succeeding series of transactions. This is primarily because each wiring, whether it occurred before or after a given act of tax fraud, served to promote and conceal each individual embezzlement of taxes, either *ex ante* or *ex post*. More precisely, each wiring, including those that occurred before a particular transaction, made it more difficult for the government to detect the entire fraudulent scheme or any particular fraudulent transaction or series of transactions. In sum, the money gained in each series of transactions (save the initial one) was the proceeds of wire fraud because the money was the proceeds of a fraud that was furthered by the prior wirings.[10]

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10. We note that this means that the funds acquired in the first series of transactions were not the proceeds of wire fraud. This is immaterial, however, since the first series, as noted above, would still constitute wire fraud, and the aggregate amount of proceeds would not be reduced significantly enough to reduce Morelli's sentence. No individual series of transactions involved more than a few hundred thousand dollars, whereas the ongoing scheme involved tens of millions of dollars. The largest single wire transfer

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Appendix A

This case is similar to *Schmuck v. United States*, 489 U.S. 705 (1989). In *Schmuck*, the Supreme Court upheld the defendant's conviction for mail fraud. The defendant had created a scheme in which he would roll back the odometers on cars and sell them as new to car dealers. As with any car sale, each unwitting dealer would mail a title-application form to the state government. The Court concluded that this mailing was sufficient to support a mail fraud conviction. In particular, the Court found that:

> Schmuck's was not a "one-shot" operation in which he sold a single car to an isolated dealer. His was an ongoing fraudulent venture. A rational jury could have concluded that the success of Schmuck's venture depended upon his continued harmonious relationship with, and good reputation among, retail dealers, which in turn required the smooth flow of cars from the dealers to their Wisconsin customers.
>
> Under these circumstances, we believe that a rational jury could have found that the title-registration mailings were part of the execution of the fraudulent scheme. . . . [A]lthough the registration-form mailings may not have

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listed in the indictment was for $780,000. Subtracting this amount from the total amount upon which Morelli's sentence was based would not change the specific offense characteristic category for the amount laundered. *See* U.S.S.G. § 2S1.1(b)(2). Accordingly, any error in including the funds from the first series of transactions was harmless.

> contributed directly to the duping of either the retail dealers or the customers, they were necessary to the passage of title, which in turn was essential to the perpetuation of Schmuck's scheme.

489 U.S. at 711-12. In *Schmuck*, the Court recognized that, even though each individual fraudulent transaction series involved a mailing only after the fraud had already been completed, each mailing contributed to the entire scheme and made each other individual fraudulent transaction series, particularly those occurring later, more likely to be successful.[11]

This case is controlled by *Schmuck*. Each wiring concealed and promoted each and every fraudulent series of transactions by making the entire scheme less detectable.

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11. We recently distinguished *Schmuck*, although not in a way that is relevant here. In *United States v. Cross*, 128 F.3d 145 (3d Cir. 1997), *cert. denied*, 118 S. Ct. 1519 (1998), we reversed mail fraud convictions based on the fact that, although the mailing at issue aided the success of the fraud, the mailing would have occurred whether the fraud had taken place or not. The alleged fraud involved fixing traffic court cases. The mailings at issue were the routine transmissions of case dispositions to the parties. We distinguished *Schmuck* on the ground that "the court regularly mailed notices to parties and the DOT in every case, whether or not the defendants had attempted to influence the result." 128 F.3d at 152 n.4. There was no causal nexus between the fraud and the mailings in *Cross*. Here, by contrast, the wirings, like the mailings in *Schmuck*, would not have been made but for the existence of the fraudulent scheme. Morelli's case is much more like *Schmuck* than *Cross*.

Without the wirings to make it appear as if a series of distinct transactions between independent companies had occurred, the taxing authorities would have had a much easier time tracking down the perpetrators of the tax fraud scheme. Each wiring "was essential to the perpetuation of [the Association]'s scheme." *Schmuck*, 489 U.S. at 712. Since each individual fraudulent series of transactions other than the initial one was preceded by a wiring that promoted it, we think that, within each transaction series, the money was the proceeds of wire fraud at the time it came into the hands of the Association in the form of the street company. As soon as one wiring took place, the entire tax fraud scheme became a wire fraud scheme. Since the very first series of transactions involved a wiring of the funds, every fraudulent acquisition of funds thereafter was an acquisition of funds through wire fraud.

This conclusion is entirely consistent with *Conley I*. *See* 37 F.3d at 980 (requiring that proceeds be "derived from an already completed offense, or a completed phase of an ongoing offense"). The entire daisy chain was an ongoing fraudulent venture. Each series of transactions within it was a "completed phase" of the ongoing scheme. As we discussed above, the phases were completed as soon as one wiring occurred as part of the entire venture and the money from the individual series of transactions came into the possession of the street company aspect of the Association.

Morelli's case also resembles *United States v. Massey*, 48 F.3d 1560 (10th Cir. 1995). In *Massey*, the defendants convinced a number of people to invest in their fraudulent loan scheme. When some of the participants became

concerned that they had not received their loans, the defendants sent them letters encouraging them not to withdraw their money. Later, one of the defendants wired some of the money to another defendant. The defendants were convicted of mail fraud and money laundering. *See* 48 F.3d at 1565. The defendants claimed that none of the money involved in the wiring came from victims who received the mailings. Accordingly, the defendants argued that the money wired could not have been the proceeds of mail fraud.

The court of appeals upheld the conviction. While noting that the defendants' assessment of the facts was correct, as far as it went, it observed that at least two mailings had been sent to victims prior to the wiring, albeit not to victims whose money was transferred in the wiring. *See* 48 F.3d at 1566. The court concluded that these mailings not only contributed to the success of the fraud with respect to the victims who received them but also to the overall success of the entire fraudulent loan program. *See* 48 F.3d at 1567 ("[T]he letters protected the plan to defraud all of the victims and not just the victim to whom the letter was sent."). In particular, if the letters had not been sent to the other victims, the fraud with respect to the victims whose money was wire transferred might not have been successful. *See* 48 F.3d at 1566-67. Accordingly,

> the jury could reasonably find that the fees deposited in the bank account from which the wire transfer was sent were derived from the fraudulent scheme that was furthered by the lulling letters. The "proceeds" of mail fraud are

> derived from the success of a fraudulent scheme that has been facilitated through the use of the mails. . . . Accordingly, we conclude that the jury had sufficient evidence to conclude that the government met all of the elements of money laundering. . . .

48 F.3d at 1567 (citations omitted).

We find *Massey* persuasive. Moreover, Morelli's case is indistinguishable from *Massey*. Had some or all of the wirings not occurred, some of the daisy chain transaction series might have been detected by the taxing authorities and the entire scheme would have been discovered sooner. Each of the wirings made before each individual fraudulent series of transactions contributed to the success of those transactions. As in *Massey*, the money resulting from these transactions was the proceeds of wire fraud at the time of the wire transfers. Accordingly, we conclude that the jury and the District Court had sufficient evidence to conclude that the government met all of the elements of money laundering under § 1956.[12] Therefore, we think the District

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12. Both parties in this case cite a number of other cases that they believe are relevant to the issue before us. *See, e.g., United States v. Christo*, 129 F.3d 578 (11th Cir. 1997); *United States v. Allen*, 76 F.3d 1348 (5th Cir. 1996); *United States v. Savage*, 67 F.3d 1435 (9th Cir. 1995); *United States v. Kennedy*, 64 F.3d 1465 (10th Cir. 1995); *United States v. Johnson*, 971 F.2d 562 (10th Cir. 1992). We do not believe these cases aid us in deciding the issue before us. They all involved the temporal question whether, at the time the alleged money laundering transaction occurred, the

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Appendix A

Court properly sentenced Morelli under the money laundering guideline.[13]

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money involved in the transaction was proceeds. *See, e.g., Allen*, 76 F.3d at 1362 ("In this case, the consultant fees and loans left the control of First City Bank and reached the accounts of the conspirators before the wire transfers occurred. The charged transactions distributed the proceeds among the various defendants and helped hide the fraud from First City auditors and federal regulators."); *Kennedy*, 64 F.3d at 1478 ("[T]he illegal mailings in this case involved discrete, earlier mailings by Kennedy, rather than the receipt of funds by Kennedy from his victims. It was the subsequent and distinct transfers of funds that were alleged as the separate transactions involving 'proceeds of specified unlawful activity' which constituted the alleged money laundering under § 1956."). This is the question we addressed in *Conley I*, 37 F.3d at 980 (proceeds must be "derived from an already completed offense, or a completed phase of an ongoing offense"). The question before us today, on the other hand, is the more abstract question whether the money was the proceeds of wire fraud. These cases do not help us answer that question.

13. Morelli also contends that the District Court erred in failing to grant him a downward departure because, even if the conspiracy involved money laundering, it was not within the "heartland" of money laundering. He relies on proposed amendments to the money laundering guidelines, which Congress rejected in 1995, that would have tied money laundering sentences to the offense level of the underlying specified unlawful activity. He also contends that he is entitled to a downward departure because the government charged him, unlike others who engaged in similar schemes but were prosecuted separately, with money laundering. Morelli claims that this constitutes unfair sentence manipulation.

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The District Court did grant Morelli a downward departure on the ground that the "value of the funds" adjustment under U.S.S.G. § 2S1.1(b)(2) overstated the seriousness of the money laundering that occurred. *See United States v. Morelli*, Opinion, Crim. No. 93-210, at 16-19 (D.N.J. Feb. 26, 1996). If the District Court refused to grant a larger downward departure in an exercise of its discretion, we have no jurisdiction to consider Morelli's claim. *See United States v. Khalil*, 132 F.3d 897 (3d Cir. 1997); *United States v. Miele*, 989 F.2d 659, 668 n.11 (3d Cir. 1993); *United States v. Parker*, 902 F.2d 221, 222 (3d Cir. 1990). On the other hand, if the sentencing court denied a larger downward departure because it erroneously concluded it lacked legal authority to consider a separate ground for departure, we have jurisdiction to review the sentence. *See United States v. Spiropoulos*, 976 F.2d 155, 160 n.2 (3d Cir. 1992).

In this case, however, the District Court committed no error. Despite Morelli's repeated and vociferous arguments, proposed amendments to the Sentencing Guidelines do not provide independent legal authority for a downward departure. *See United States v. Anderson*, 82 F.3d 436 (D.C. Cir. 1996) (explaining persuasively why proposed crack cocaine amendments did not provide independent authority for a downward departure). Furthermore, Morelli's invocation of *United States v. Lieberman*, 971 F.2d 989, 994-96 (3d Cir. 1992), in which we affirmed a district court's grant of a downward departure for manipulation of the indictment, does not help him since in that case the district court had decided in its discretion that a downward departure was appropriate and the question on appeal was whether the district court had authority to do so. Here, by contrast, the District Court considered both of Morelli's proposed grounds for departure and exercised its discretion to reject them. Accordingly, since Morelli's argument is essentially a challenge to the District Court's exercise of its discretion in denying him an additional downward departure, we have no jurisdiction to consider his claim.

Appendix A

III. Roizman's Appeal

Roizman argues that his conviction should be reversed because of an actual or potential conflict in his attorney's representation of both him and one Igor Porotsky. Porotsky was neither a codefendant nor a witness at trial, but his statements were admitted as hearsay statements through the testimony of other witnesses. In particular, various witnesses testified that Porotsky had been involved in the fuel business before the Association was created, and that he had been involved with Morelli and other alleged members of the Italian Mafia. At the time of trial, Larry Silverman, who was then Roizman's attorney, was also representing Porotsky in a separate matter.[14] Roizman argues that, as a result of this representation, Silverman suffered a conflict and was unable to impeach Porotsky as a hearsay declarant adequately. *See* Fed. R. Evid. 806 (permitting impeachment of the declarant of statements admitted as hearsay). Roizman also contends that, even if this was only a potential conflict, it merits a reversal because counsel for the government should have been aware of it at trial.

After we remanded Roizman's claims to the District Court, the Court heard arguments and considered the documentary evidence. For the reasons set forth *infra*, the

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14. We need not consider the much-debated issue of the precise scope of this representation, however, since we conclude that, regardless of the scope of the representation, cross-examining Porotsky was not a useful alternative strategy and, at all events, doing so would not have conflicted with Silverman's duties to Porotsky.

District Court rejected all of Roizman's claims regarding Silverman's representation and alleged conflict of interest. "We apply plenary review to the district court's application of legal precepts, and clearly erroneous review to its factual findings." *United States v. Brink*, 39 F.3d 419, 421 (3d Cir. 1994) (citations omitted).

A. Actual Conflict of Interest

An actual conflict claim arises after trial upon the discovery of a previously unnoticed conflict of interest on the part of trial counsel. "[A] defendant who raised no objection at trial must demonstrate that an actual conflict of interest adversely affected his lawyer's performance." *Cuyler v. Sullivan*, 446 U.S. 335, 348 (1980). We have elaborated on this as follows: "An actual conflict of interest 'is evidenced if, during the course of the representation, the defendants' interests diverge with respect to a material factual or legal issue or to a course of action.' " *United States v. Gambino*, 864 F.2d 1064, 1070 (3d Cir. 1988) (quoting *Sullivan v. Cuyler*, 723 F.2d 1077, 1086 (3d Cir. 1983)). In addition, we have noted that an actual conflict is more likely to be found where "an attorney takes positive steps on behalf of one client prejudicial to another" as opposed to cases where "the attorney's actions are based on inaction and are passive." *Gambino*, 864 F.2d at 1070.

Similarly, an actual conflict is more likely to occur in cases of joint representation — representation of more than one defendant at the same trial — rather than simply multiple representation — representation of defendants in different trials — as occurred here. In cases involving

multiple but not joint representation, and when an attorney has in some way failed to act, we have adopted the following standard:

> In order to establish an actual conflict the petitioner must show two elements. First, he must demonstrate that some plausible alternative defense strategy or tactic might have been pursued. He need not show that the defense would necessarily have been successful if it had been used, but that it possessed sufficient substance to be a viable alternative. Second, he must establish that the alternative defense was inherently in conflict with or not undertaken due to the attorney's other loyalties or interests.

Gambino, 864 F.2d at 1070 (quoting *United States v. Fahey*, 769 F.2d 829, 836 (1st Cir. 1985)); *see also Hess v. Mazurkiewicz*, 135 F.3d 905, 910 (3d Cir. 1998). When an actual conflict with an adverse effect, of the sort described above, is demonstrated, the defendant is entitled to a reversal for inadequate assistance of counsel without demonstrating prejudice. *See Strickland v. Washington*, 466 U.S. 668, 692 (1984).[15]

The District Court found no actual conflict in Silverman's representation of both Porotsky and Roizman. In particular, the court found that Silverman's decision not

15. Of course, if the defendant cannot prevail on an actual conflict theory, the defendant can still bring a conventional ineffective assistance claim under *Strickland*, but the defendant must then show prejudice. *See Hess*, 135 F.3d at 910.

to attempt to impeach Porotsky was a reasonable strategic decision:

> In this case, it is abundantly clear from an examination of Mr. Roizman's claim in the larger context of the trial that cross-examination of Mr. Porotsky was not a plausible defense strategy that "possessed sufficient substance" to raise a claim of constitutional dimension. . . .
>
> The Court's observations during the lengthy trial confirm that Mr. Roizman's attorney pursued a "wallflower" defense — that is, that Mr. Roizman was an innocent operator who was a victim of intimidation from other organized crime figures. To have vigorously cross-examined Porotsky, a witness whose hearsay testimony was cumulative and peripheral, and to therefore have risked creating in the jurors' minds a connection between Porotsky and Roizman, would have been asinine in light of the strategy Mr. Roizman pursued. The Court, drawing on its observation of the strategy employed during the trial, as well as Mr. Silverman's affidavit submitted herewith, concludes that the decision not to cross-examine Mr. Porotsky's hearsay statements was not tainted by a conflict of interest. Rather, it was a sound decision, based on an experienced trial lawyer's strategic considerations.

United States v. Morelli, Opinion & Order, Crim. No. 93-210, at 7-8 (D.N.J. Oct. 16, 1997). As the District Court also noted, this strategy was quite successful: "Of the eighteen counts in the indictment against Mr. Roizman, he was acquitted of 13, including the global conspiracy charge." *Id.* at 7 n.5.

Roizman alleges that Porotsky's hearsay statements incriminated him in several ways. The District Court rejected this argument, finding that impeaching Porotsky would have made Roizman's "wallflower defense" less successful. *See id.* at 7. It also concluded that Porotsky's statements were "so cumulative and peripheral" that impeaching them would have at best made no difference. Based on our review of the record, we find that the District Court's conclusions were probably correct, and certainly not clearly erroneous. Based on these facts, we agree with the District Court's conclusion that cross-examination of Porotsky was not an alternative strategy with "sufficient substance to be a viable alternative." *Gambino*, 864 F.2d at 1070.

Even if we were to conclude that the District Court did clearly err in its conclusions on the previous point, we would still affirm its rejection of Roizman's claim. We do not believe that the alleged alternative strategy of impeaching Porotsky created a conflict between Silverman's duties to Roizman and Porotsky. The key point, and one only recognized in *Gambino* as far as we can tell, is that we must look at the attorney's duties to both clients. An actual conflict exists only if the proposed alternative strategy (a) could benefit the instant defendant and (b) *would violate*

the attorney's duties to the other client. See Gambino, 864 F.2d at 1070.

In *Gambino*, the court rejected the defendant's actual conflict claim because it found that the proposed strategy would not have hurt the attorney's other client. *Gambino* involved a drug distribution charge. The defendant (Gambino) claimed that his attorney could have argued that another of the attorney's clients, Mazzarra, might have committed the crime with which Gambino was charged. But Mazzarra was not a codefendant, and the proposed argument would not have rendered Mazzarra directly liable to punishment. Furthermore, the information Gambino contended would have supported the strategy came from the government's files. Exposing this evidence at trial would not have given the government any new information that would have made it more likely to charge Mazzarra. The court concluded that no actual conflict existed because "Mazzara would not have been prejudiced if Evseroff [the attorney] had [tried to show he was the source of the heroin] and thus it follows that appellant and Mazzara did not have conflicting interests in Evseroff's performance at trial." *Gambino*, 864 F.2d at 1071.

We think that this case is analogous to *Gambino*. Porotsky was not a defendant in Roizman's case. While Porotsky probably would not have wanted to be impeached as a criminal, he had been convicted of various crimes, and numerous other witnesses at trial had discussed his criminal activities. (In fact, the impeachment would have involved almost exclusively the evidence of these convictions.) Furthermore, the evidence Silverman would have used to

impeach Porotsky's statements — including Porotsky's prior convictions and present indictments — would most likely have come from the government. We do not see how exposing such information, already in the possession of the government, could have harmed Porotsky's interests.[16]

B. Potential Conflict of Interest

Roizman also claims that his conviction should be reversed under a potential conflict theory. We reject this claim as well.

When a district court is aware, or should be aware, of a potential conflict of interest on the part of the defendant's attorney, the court must inquire as to whether the defendant is aware of and waives this conflict. *See Wheat v. United States*, 486 U.S. 153 (1988); *Wood v. Georgia*, 450 U.S. 261, 272 (1981); *United States v. Pungitore*, 910 F.2d 1084, 1143 (3d Cir. 1990). Roizman argues that reversal is required not only when the trial court is aware of such a conflict and fails to act but also when the prosecutor and defense attorney are aware of one. Although Roizman cites

16. Roizman also suggests that Silverman should have used information he acquired from Porotsky during his representation of him to impeach Porotsky. We reject this contention. If Silverman had not represented Porotsky and thus created the alleged conflict of interest in this case, he would not have had access to this information. Roizman cannot prevail on the argument that his interests were harmed by Silverman's failure to use information he acquired in confidence from Porotsky to impeach Porotsky. Accordingly, we conclude that no actual conflict with Silverman's duties to Porotsky affected his representation of Roizman.

several cases from courts within the Second Circuit in support of this claim, *see, e.g., United States v. Rahman*, 861 F. Supp. 266, 278 (S.D.N.Y. 1994), the court of appeals in that circuit has at most only exhorted prosecutors to advise the trial courts when they are aware of conflicts, *see United States v. Stantini*, 85 F.3d 9, 13 (2d Cir. 1996). *See also Cerro v. United States* 872 F.2d 780, 787 (7th Cir. 1989) ("We do not disagree with the propriety of such a recommendation under like circumstances, but we conclude that it is not a constitutional requirement. In the present case, the prosecutor was under no constitutional duty to advise the trial court of a potential conflict based on the information available to him."). They have not held, and we do not hold, that a prosecutor's — or a defense attorney's — failure in this respect is grounds for reversal. Since Roizman makes no claim that the District Court was or should have been aware of Silverman's potential conflict, he is not entitled to a reversal on these grounds.[17]

17. Finally, Roizman argues that we should reverse the District Court's decision because it failed to conduct an evidentiary hearing on his claims. Because we conclude that the District Court did not err in rejecting Roizman's claims based on the documentary evidence before it, we see no need for the court to have conducted further evidentiary proceedings.

For all these reasons, the judgments of the District Court with respect to both Morelli and Roizman will be affirmed.

A True Copy:
Teste:

Clerk of the United States Court of Appeals
for the Third Circuit

APPENDIX B — JUDGMENT OF THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT DATED MARCH 9, 1999

IN THE UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

NOS. 96-5144 and 96-5389

UNITED STATES OF AMERICA

v.

MORELLI, ANTHONY
(D.C. Crim. No. 93-cr-00210-1)
Appellant in No. 96-5144

(Amended per Clerk's order of 7/8/98)

UNITED STATES OF AMERICA

v.

IGOR ROIZMAN, a/k/a Little Igor
(D.C. Crim. No. 93-cr-00210-10)
IGOR ROIZMAN, Appellant in No. 96-5389

Present: Becker, *Chief Judge*, Scirica, *Circuit Judge*, and Kelly, *District Judge**

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* Honorable James McGirr Kelly, United States District Judge for the Eastern District of Pennsylvania, sitting by designation.

Appendix B

JUDGMENT

These causes came on to be heard on the record from the United States District Court for the District of New Jersey and were argued by counsel on June 5, 1997 and reargued September 8, 1998.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgments of the said District Court entered March 5, 1996 as to Anthony Morelli and June 18, 1996 as to Igor Roizman, be, and the same are hereby affirmed. All of the above in accordance with the opinion of this Court.

ATTEST:

s/ P. Douglas Sisk
Clerk

Dated: March 9, 1999

APPENDIX C — OPINION OF THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY DATED AND FILED FEBRUARY 26, 1996

UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF NEW JERSEY

Crim. No. 93-210 (WGB)

UNITED STATES OF AMERICA,

Plaintiff,

v.

ANTHONY MORELLI, et al.,

Defendants.

OPINION

* * *

BASSLER, DISTRICT JUDGE:

The Defendant, Anthony Morelli, presents a number of objections to the Presentence Investigation Report ("PSR"). In addition, Morelli requests a downward departure from the applicable sentencing guidelines pursuant to U.S.S.G. §5K2.0. For the following reasons, the Court will grant his application in part and adjust his sentence accordingly.

Appendix C

I. BACKGROUND

Defendant Morelli was a participant in a scheme to evade federal and state excise taxes on the sale of gasoline and diesel fuel. The scheme capitalized on the way in which the government collected federal excise taxes during the time in question. At that time, wholesale distributors could sell the fuel on a tax exempt basis if they obtained an IRS Form 637 (Registration For Tax Free Transactions). The IRS Form 637 enabled one wholesale distributor with a 637 to sell motor fuel to another wholesale distributor with a 637 without having to pay excise tax. Once a wholesale distributor sold the fuel to an entity that did not possess a Form 637, the distributor became liable for the tax. It was common industry practice for the last wholesaler to include the tax amount in the price charged the non-registered purchaser. Subsequently, the wholesaler would remit the tax to the IRS on a quarterly basis.

The tax evasion scheme in which Morelli participated "involved the use of 'daisy chains', a series of paper transactions through numerous companies, some of which were largely fictitious." *United States v. Veksler*, slip op. No. 94-1982 (3d Cir. August 9, 1995). In each daisy chain, the first company has a valid form 637 and thus, would purchase fuel tax free. After purchasing the fuel, the company would pretend to sell the fuel in a series of paper transactions. At some point in the daisy chain a company with a fraudulent 637, the "burn" or "butterfly" company, would appear to purchase the fuel on a tax free basis. The burn company would produce invoices to its purchaser indicating that the tax had been paid and charge the

purchaser a tax included price. The conspirators continued to sell the fuel down the chain in further paper transactions. Ultimately, the last company in the daisy chain would sell the fuel to a retailer. The conspirators would then wire the money from the sale of the fuel back up through the companies in the daisy chain.

The "burn" or "butterfly" company would disappear after a short period of time. When the IRS investigated the tax shortages, the company above the burn company in the chain would produce a copy of the burn company's form 637, indicating that it was proper for the company above the burn company to sell the fuel on a tax exempt basis. The company below the burn company would produce invoices reflecting that the tax had been paid by the burn company and that the burn company sold the fuel to it on tax included basis. Because the burn company was a fictitious entity which had disappeared, the IRS could not collect the tax money.

In order to unravel the scheme, the government created an undercover business selling bootleg fuel.

The bootleg fuel sales generated substantial profits. Four organized crime families active in the Northern New Jersey-New York Metropolitan area, the Gambino, Genovese, Lucchese, and Columbo families, coordinated their activities and shared the profits from their extortionate control over the bootleg motor fuel industry.

Defendant Anthony Morelli was a representative of the Gambino crime family. He acted as a captain of the family;

each captain supervised and controlled the activities of one or more groups or crews of individual "soldiers" or members of the family. Morelli represented the family in extorting a "mob tax" or pitulation from individuals involved in the bootleg sale of motor fuel. Morelli was responsible for forwarding this money to the "boss" of the Gambino crime family.

Morelli was indicted in a forty-two count Second Superseding indictment. The jury convicted Morelli of a RICO conspiracy, RICO, an extortion conspiracy, extortion of the undercover business, mail fraud, and conspiracy. With respect to Count 1 (RICO conspiracy), the jury found that the government had proven the following racketeering acts as to Morelli: Racketeering Acts 1 and 2 (Extortion); 3-7 (Wire Fraud and Money Laundering); 8 (Wire Fraud); and 9-12, 14-15, and 18-20 (Mail Fraud). With respect to Count 23 (conspiracy) the jury found that the objects of the conspiracy were wire fraud, mail fraud, and money laundering.

Morelli was not named in any of the Racketeering Acts alleging money laundering. His liability for those acts is apparently based on the jury's determination that (i) he had agreed to be a member of the RICO conspiracy; (ii) his coconspirators agreed that money laundering offense would be committed in furtherance of the conspiracy; and (iii) the commission of the money laundering offenses was foreseeable.

In calculating Morelli's guideline offense level, the PSR separates the crimes on which the jury returned a verdict of

guilty into three groups: Fraud, Extortion and Money Laundering. In the fraud group, the PSR calculates a base offense level of 6. It increases that level by 18 based on a tax loss in excess of $99 million, 2 for more than minimal planning and 4 for Morelli's role as a leader or organizer of the offense. Thus, the total offense level for the fraud counts is 30.

In the extortion category, the PSR uses a base offense level of 18, then adds 2 points for "implied threat of bodily harm" and 4 points for Morelli's role in the offense as a leader or organizer. Thus, the total extortion offense level is 24.

In the money laundering category, the PSR uses a base offense level of 23, to which it adds 12 points for funds exceeding $60 million and 4 points for Morelli's role in the offense as a leader or organizer. The total money laundering offense level is 39.

Because the highest offense level, 39, is 9 or more levels above the other two groups, the level is not increased to include the other groups. Thus, the PSR calculates Morelli's sentence as 324-405 months based on a total offense level of 39 and a criminal history category of III.

II. DISCUSSION

Morelli raises the following objections to the PSR: (1) Morelli argues that as a matter of law, the conspirators did not commit money laundering; (2) Morelli objects to the 4 level increase pursuant to 3B1.1(a) for his role as an

organizer or leader of the conspiracy; (3) Morelli challenges the calculations of both the amount of money involved in the laundering and the amount of money involved in the fraud, which result in a 12 level increase for money laundering and an 18 level increase for fraud; (4) Morelli objects to the 2 level increase pursuant to 2B3.2(b)(1) for an offense involving an implied threat of bodily harm.

A. Application of Money Laundering Guidelines

The money laundering statute, 18 U.S.C. sec. 1956, provides in relevant part:

> Whoever, knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity, conducts or attempts to conduct such a financial transaction which in fact involves the proceeds of specified unlawful activity — (A)(i) with the intent to promote the carrying on of specified unlawful activity or (ii) with intent to engage in conduct constituting a violation of section 7201 or 7206 of the Internal Revenue Code of 1986; or (B) knowing that the transaction is designed in whole or in part — (i) to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity . . . [is guilty of money laundering].

Morelli argues that as a matter of law, money laundering did not occur because the allegedly "laundered" funds were not the proceeds of a specified unlawful activity.

Appendix C

The indictment alleges money laundering in sets of three counts. After receiving money from the retailer, the defendants wired the money back up the daisy chain. In the Second Superseding Indictment, the first wiring up the daisy chain is characterized as wire fraud[1] and the next wiring as money laundering. *See* Counts 24-26, 27-29, 30-32, 33-35, 36-38. Wire fraud is a "specified unlawful activity". 18 U.S.C. sec. 1956(b)(7); 18 U.S.C. sec. 1961(1). The government contends that the funds in the second wiring were proceeds of the wire fraud.

18 U.S.C. sec. 1956 does not define the term "proceeds." Black's Law Dictionary defines proceeds as "[t]hat which results, proceeds, or accrues from some possession or transaction." 1204-05 (6th ed. 1990). Although recognizing that the statute does not specify when money becomes proceeds, the Third Circuit indicates that "proceeds are derived from an already completed offense, or a completed phase of an ongoing offense . . ." *United States v. Conley*, 37 F.3d 970, 980 (3d Cir. 1994). "Congress aimed the crime of money laundering at conduct that follows in time the underlying crime rather than to afford an alternative means of punishing the prior 'specified unlawful activity." *United States v. Edgmon*, 952 F.2d 1206, 1214

1. The wire fraud statute, 18 U.S.C. sec. 1343, provides: "Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, transmits or causes to be transmitted by means of wire, radio, or television communication in interstate or foreign commerce, any writings, signs, signals, pictures, or sounds for the purpose of executing such scheme or artifice, shall be fined under this title or imprisoned not more than five years, or both."

(10th Cir. 1991) cert. denied 505 U.S. 1223 (1992). *See also United States v. Johnson*, 971 F.2d 562, 569 (10th Cir. 1992).

Morelli argues that the money involved in the wire transfers constitutes proceeds of legitimate fuel sales, not proceeds of the wire fraud. He contends that the conspirators did not gain anything from the first wire transfer, and thus, did not earn any "proceeds" from the wire fraud. Morelli also argues that until the burn company disappears with the money, there are no illegal proceeds because the taxes could have been paid.

The court concludes that the funds involved in the second wire transfer are "proceeds" of the wire fraud within the meaning of 18 U.S.C. §1956. The use of wire transfers to move large amounts of cash from the sale of bootleg fuel was not a random, accidental event, but an important part of the daisy chain. The transfer of money, which included unpaid taxes, was critical to the success of the scheme. The transfer of the wire fraud proceeds through companies that were ostensibly legitimate businesses was designed to disguise the fact that motor fuel taxes were not being paid.

Once the wired funds were deposited, the funds became proceeds of the defendants' wire fraud; the subsequent transfers were designed to promote illegal activity or conceal the nature of the funds, and thus, were money laundering. Consequently, the money laundering guidelines are applicable to Morelli's sentence.

Appendix C

B. Calculation of Amount Laundered

U.S.S.G. 2S1.1(a)(1) indicates that the base offense level for money laundering in violation of §1956(a)(1)(A) is 23. §2S1.1(b)(2) provides for an increase in the offense level based upon the "value of the funds laundered." The PSR lists a 12 level increase because the value of the funds exceeded $60 million.

"The calculation of 'the value of the funds' under §2S1.1(b)(2) includes the aggregate of all funds involved in the money laundering scheme without regard to either the 'actual loss' which the victim suffered or the return of any monies to the victims." *United States v. Thompson*, 40 F.3d 48, 52 (3d Cir. 1994) cert. denied 115 S.Ct. 1390 (1995).

Morelli argues that the only amount that the government proved was laundered is the amount charged in the indictment, a total of $1,155,000. Second Superseding Indictment Counts 25, 26, 28, 29, 31, 32, 34, 35, 37, 38. The government, however, is not limited to the amount charged in the Indictment. Under the relevant conduct provisions, U.S.S.G. §§ 1B1.3(a)(1) and 3D1.3(b), the court is required to consider the entire amount, whether or not specifically charged. *See United States v. Rose*, 20 F.3d 367, 371 (9th Cir. 1994) ("the Sentencing Guidelines require rather than prohibit consideration of conduct beyond the counts on which a defendant was convicted"); *United States v. Mullens*, 65 F.3d 1560, 1564 (11th Cir. 1995) ("a sentencing court is 'required to consider the total amount of the funds that it believed was involved in the course of criminal conduct").

Appendix C

The government contends that its figure of $65,841,211 is based upon the total dollar amount transferred up the daisy chain by the bottom companies for diesel fuel only. Morelli argues that the government's figure is inaccurate because it has not established that the money was subsequently re-wired, and thus, laundered.

Revenue Agent Paul Malloy credibly testified that the defendants wired $65,841,211 in proceeds from the sale of diesel fuel from the bottom companies in the daisy chain back up the chain. Malloy also testified that he traced the wired funds through subsequent financial transactions. The government has established by a preponderance of the evidence that the defendants subsequently used the funds to promote the scheme and or took steps to conceal them. Consequently, under 2S1.1(b)(2), $65,841,211 is the value of the funds laundered.

C. Role in Offense

3B1.1(a) provides for a four level increase "[i]f the defendant was an organizer or leader of a criminal activity that involved more than five participants." 3B1.1(b) provides for a three level increase if "the defendant was a manager or supervisor (but not an organizer or leader) and the criminal activity involved five or more participants or was otherwise extensive." The PSR provides for a four level increase in each group: fraud, extortion and money laundering.

Morelli contends that his role in the offense does not warrant any increase in the offense level. He also argues

that even if the enhancement is applicable to the extortion group, it does not apply to the fraud and money laundering groups.

The introductory commentary to 3B indicates that "[t]he determination of the defendant's role in the offense is to be made on the basis of all conduct within the scope of §1B1.3 (Relevant Conduct), *i.e.* all conduct included under §1B1.3(a)(l)-(4) and not solely on the basis of elements and acts cited in the count of conviction." §1.B1.3(a) provides that in the case of jointly undertaken criminal activity, the court may consider "all reasonably foreseeable acts and omissions of others in furtherance of the jointly undertaken criminal activity." Both guidelines refer to the defendant's role in a "criminal activity", as opposed to a specific crime. Thus, the court must focus on the conspiracy as a whole in determining Morelli's role, and any enhancement will apply to all of the groups. *See, e.g. United States v. Patriarca*, 807 F.Supp 165, 180-82 (D.Mass. 1992), *vacated on other grounds sub nom. United States v. Carozza*, 4 F.3d 70 (1st Cir. 1993), *cert. denied*, 114 S.Ct. 1644 (1994).

The Commentary to 3B1.1 indicates that the court should consider the following factors in distinguishing leaders and organizers from supervisors and managers: "the exercise of decision making authority, the nature of participation in the commission of the offense, the recruitment of accomplices, the claimed right to a larger share of the fruits of the crime, the degree of participation in planning or organizing the offense, the nature and scope of the illegal activity, and the degree of authority and control exercised over others."

Morelli played a significant role in the conspiracy. He adjudicated disputes and at times determined who would participate in the daisy chains and who would be excluded. *See e.g.*, Trial Transcript at 4375-76, 4400-07, 4291-92, 4378-81, 4427, 4573. Morelli also made significant decisions regarding what wholesalers should be told not to do business with the undercover business and approved who should contact the undercover business. Morelli designated much of the routine decisionmaking to Dougherty, who reported directly to Morelli. *See, e.g.* Trial Transcript at 5073-75; 4519; 4762-64; 4417-18.

Nevertheless, the testimony does not establish that Morelli was an organizer or leader of the conspiracy. Although he played a significant role, in considering the factors identified in the commentary to 3B1.1, the court concludes that Morelli's function was as a supervisor or manager of the scheme. Thus, the court will use a 3 point increase rather than a 4 point increase for Morelli's participation in the scheme.

D. Calculation of the Fraud Loss

2F1.1(b) provides for an increase in the offense level for fraud based on the loss. The PSR provides for an 18 point increase because the fraud loss exceeded $80 million dollars. Morelli argues that the $99 million tax loss figure asserted by the government was not established at trial.

"[F]raud 'loss' is, in the first instance, the amount of money the victim has actually lost (estimated at the time of sentencing), not the potential loss as measured at the time

of the crime." *United States v. Kopp*, 951 F.2d 521, 536 (3d Cir. 1991). Revenue Agent Paul Malloy testified that the lost federal tax revenue was $77,738,605. Trial Transcript at 9875. New Jersey State Revenue Agent Albert Lugg testified that the evaded state tax was $21,907,734. The total figure $99,646,339, exceeds $80 million. Morelli did not challenge the testimony. Accordingly, the 18 level increase for a tax loss of greater than $80 million pursuant to 2F1.1(b)(1)(S) is appropriate.

E. Implied Threat of Bodily Harm

The PSR provides for a two level increase in the extortion group pursuant to 2B3.2(b)(1). 2B3.2(b)(1) provides "[i]f the offense involved an express or implied threat of death, bodily injury, or kidnapping, increase by 2 levels." Morelli argues that there was no implied threat of bodily harm, thus a 2 level increase is not warranted.

2B3.2(b)(1) Note 2 explains:

> This guideline applies if there was any threat, express of implied, that reasonably could be interpreted as one to injure a person or physically damage property, or any comparably serious threat, such as to drive an enterprise out of business. Even if the threat does not in itself imply violence, the possibility of violence or serious adverse consequences may be inferred from the circumstances of the threat or the reputation of the person making it. An ambiguous threat, such as "pay up or else," or a

> threat to cause labor problems, ordinarily should be treated under this section.

The daisy chain conspiracy produced several threats encompassed by 2B3.2(b)(1). Other than the general threat of organized crime involvement, there were specific threats. For example, Morelli's associates told Zeidenfeld, a customer of the undercover business, to stop buying fuel from the undercover business. At the time, Dougherty, who worked directly for Morelli, told Zeidenfeld that if Dougherty hadn't been there Zeidenfeld "would have had a problem." Trial Transcript at 4520. Dougherty told Zeidenfeld that he should "go back and tell the undercover business that we're only a heartbeat away." *Id.*

Dougherty subsequently met with two undercover agents and told them that their other two partners "almost got hurt". Trial Transcript at 5797. Dougherty explained that the message was for the agents to "get on board with us or stay out of business." *Id.* He indicated that if they did not accept, they would have been paid a "visit" which would have included violence. *Id.* Morelli has not explained why this testimony does not constitute a threat. Accordingly, the court finds that a 2 level increase for an implied threat of bodily harm pursuant to 2B3.2(b)(1) is warranted.

F. Downward Departure

Finally, Morelli argues that the Court should depart from the guidelines under §5K2.0. Essentially, Morelli argues that by applying the money laundering guidelines, the court is doubly punishing the defendants for their

participation in a complex tax fraud scheme. According to Morelli, the defendants intended to commit tax fraud, but did not intend to launder money and thus, should be sentenced under the fraud guidelines.

Downward departure is discretionary for the district court. *United States v. Frazier*, 981 F.2d 92, 96 (3d Cir. 1992) cert. denied 507 U.S. 1010 (1993); *United States v. Georgiadis*, 933 F.2d 1219, 1222 (3d Cir. 1991). "The Commission intends sentencing courts to treat each guideline as carving out a "heartland", a set of typical cases embodying the conduct that each guideline describes. When a court finds an atypical case, one to which a particular guideline linguistically applies but where conduct significantly differs from the norm, the court may consider whether a departure is warranted." Ch. 1, Pt. A, 4(b).

The Guidelines permit a district court to depart where "there exists an aggravating or mitigating circumstance of a kind, or to a degree not adequately taken into consideration by the Sentencing Commission in formulating" the applicable Guidelines. U.S.S.G. §5K2.0; 18 U.S.C. sec. 3553(b). The Guidelines also indicate that "the court may depart from the guidelines, even though the reason for departure is taken into consideration in the guidelines (*e.g.*, as a specific offense characteristic or other adjustment), if the court determines that, in light of unusual circumstances, the guideline level attached to that factor is inadequate." 5K2.0.

Morelli argues that the court should not apply the money laundering guidelines because all "daisy chain" tax fraud

schemes inherently include money laundering. This argument is without merit. "Congress designed the (money laundering) statute to fill 'the gap in the criminal law with respect to the post-crime hiding of ill-gotten gains,' and intended money laundering to be a separate crime distinct from the underlying offense that generated the money." *United States v. LeBlanc*, 24 F.3d 340, 346 (1st Cir. 1994) cert. denied sub nom. 115 S.Ct. 250 (1994). Fraud and money laundering are distinct offenses with different elements. Contrary to Morelli's argument, the defendants could have engaged in tax fraud without laundering the money. Here, the defendants created an elaborate scheme to not only defraud the government, but to conceal the funds and promote the commission of further offenses by wiring the money back up the daisy chain.

Morelli did engage in money laundering, however the court finds that the "daisy chain" scheme is outside of the heartland of the money laundering guidelines. Specifically, the court finds that the 12 level enhancement under 2S1.1(b) for the $65,841,211 value of the funds laundered overrepresents the seriousness of the crime. Although technically the entire $65 million dollars constitutes proceeds of the wire fraud, most of that money represents money from the sale of fuel; only a small percentage of the money constitutes the illegally obtained tax revenue.

The commentary to 2S1.1 indicates that "[t]he amount of money involved is included as a factor because it is an indicator of the magnitude of the criminal enterprise, and the extent to which the defendant aided the enterprise." But the amount collected overrepresents the harm because not

all of the money collected was money due the U.S. government. While the total proceeds represents the total amount collected, it isn't coextensive with the actual loss inflicted.

Although the commentary to 2S1.1 does not specifically authorize departures where the value of the funds overstates the seriousness of the offense, the guideline is analogous to 2F1.1 (Fraud and Deceit). Like 2S1.1 which increases the offense level based on the value of the laundered funds, 2F1.1(b)(1) increases the offense level based on the amount of fraud loss. The Commentary to 2F1.1 (Fraud and Deceit) authorizes an upward departure where the loss is underrepresented and also recognizes that "[i]n a few instances, the loss determined under subsection (b)(1) may overstate the seriousness of the offense." 2F1.1 Application Note 10.

The daisy chain scheme is unlike the typical money laundering case in which all of the laundered money is generated by illegal activity, such as illegal gambling or the sale of drugs. *See e.g. United States v. Conley*, 37 F.3d 970 (3d Cir. 1994). The scheme is also not the typical wire fraud case in which a defendant induces investors to participate in an illegitimate investment, such as a ponzi scheme, and then launders the invested funds. *See, e.g. Mullens*, 65 F.3d at 1564-65. In those types of cases, all of the money is obtained illegally. In contrast, in the "daisy chain" scheme, only part of the funds obtained from the retailers and transferred up the chain represent illegal profits, the unpaid taxes. The rest of the money represents funds from the sale of legitimate products. The fraud is on the

government, not the purchasers; the purchasers get what they pay for.

The court finds that in a "daisy chain" case, although all of the funds involved in the wire transfers are technically proceeds of the wire fraud, the appropriate amount on which to base the "value of the funds" calculation is the amount of tax revenue that the defendants laundered. I find the testimony of Revenue Agent Paul Malloy credible. Malloy testified that of the $65,841,211 dollars involved in the wire fraud, only $14,087,694 constitutes illegally obtained state tax revenue.[2]

Malloy calculated the tax revenue in the following manner: The defendants wire transferred $65,841,211 dollars from the bottom companies in the daisy chain back up the chain. At trial, Malloy testified that the price per gallon for retailers was approximately 67 cents. Trial Transcript at 9825. Agent Monks testified that the retailers wanted to pay "60 to 65 cents, or 70 cents depending on the market." *Id.* at 8299. Using a figure of $0.67 cents per gallon, Malloy computes that the wired money represents the sale of 98,270,464 gallons. New Jersey imposed two types of taxes on the sale of diesel fuel, an excise tax and a gross receipts tax. Malloy calculates that $14,087,694 is the amount of New Jersey state tax revenue on the sale of

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2. The government indicates that due to a Department of Justice policy, it bases the money laundering charges solely on lost New Jersey state tax revenue from the sale of diesel fuel. The court calculates that in addition to the state taxes, the defendants laundered $19,217,958 in federal excise taxes.

diesel fuel included in the $65,841,211 that was laundered by the defendants.[3]

Under 2S1.1, a value of laundered funds of more than $10 million but less than $20 million merits a 9 level increase. Thus, the court will downward depart 3 levels from a 12 level increase for a value exceeding $60 million to a 9 level increase for a value of between $10 and $20 million. The new offense level for money laundering is 35. Under 3D1.4, the court must add 1 level to the money laundering offense level because the offense level for the fraud group, 29, is between 5 and 8 levels less serious than the offense level for money laundering. Thus, the total combined offense level is 36.

III. CONCLUSION

For the reasons explained above, the Court finds that Morelli's base offense level for money laundering is 23, that the guidelines provide for a 12-level increase for laundering funds in excess of $60 million dollars under § 2S1.1(b)(2), and a 3-level increase for his role as a manager/supervisor of the scheme, resulting in a total offense level of 38.

The PSR indicates that Morelli's criminal history category is III, which Morelli does not contest. Under the

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3. The calculation of the tax loss need not be precise. *See, e.g.* 2B1.1 (Larceny, Embezzlement, and Other Forms of Theft) Application Note 3 ("[L]oss need not be determined with precision. The court need only make a reasonable estimate of loss, given the available information."); 2F1.1 Application Note 7.

sentencing table, a defendant with an offense level of 38 and a criminal history category of III has an applicable sentencing range of 292-365 months.

The court finds, however, that the "daisy chain" scheme is outside of the heartland of the guidelines and the $65,841,211 value of the funds laundered under 2S1.1(b)(2) overstates the seriousness of the offense. The court awards Morelli a downward departure of 3 levels based on a calculation that the unpaid tax of $14,087,694 more appropriately reflects the seriousness of the money laundering offense. Thus, the new offense level for money laundering is 35. Under 3D1.4, the court must add one level to represent the fraud group. Thus, the new combined offense level is 36. The sentencing range for an offense level of 36 and a criminal history of III is 235-293 months.

Dated: February 26th, 1996

s/ William G. Bassler
WILLIAM G. BASSLER, U.S.D.J.

APPENDIX D — JUDGMENT IN A CRIMINAL CASE OF THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY DATED AND FILED MARCH 1, 1996

UNITED STATES DISTRICT COURT
DISTRICT OF NEW JERSEY

UNITED STATES OF AMERICA

VS.

ANTHONEY MORELLI

(Defendant's Name)

JUDGMENT IN A CRIMINAL CASE

(For Offenses Committed On or After November 1, 1987)

Case Number: 93-210-01

RICHARD REHBOCK, ESQ.
Attorney's Name

THE DEFENDANT:

____ plead guilty to count(s) _____.

__X__ was found guilty on count(s) 1,2,3,4,11,12,13,14, 16,17,20,21,22 & 23 after a plea of not guilty.

Appendix D

Accordingly, the defendant is adjudged guilty of such count(s) which involve the following offenses:

Title Section	Nature of Offense	Date of Offense	Counts
18:1962(d)	RICO Conspiracy	October 1991	1
18:1962(c)	RICO	"	2
18:1951 & 2	Extortion	"	3 & 4
18:1341 & 2	Mail Fraud	"	11-14,16, 17 & 20-22
18:371	Money Laundering Conspiracy	"	23

The defendant is sentenced as provided in pages 2 through 4 of this judgment. The sentence is imposed pursuant to the Sentencing Reform Act of 1984.,

__X__ The defendant has been found not guilty on counts 15, 18 & 19 and is discharged as to such count(s).

__X__ Count(s) 5 was dismissed on the motion of the United States at Trial.

__X__ It is ordered that the defendant shall pay a special assessment of $50.00, for count(s) 1-4,11-14,16,17, 20-22 & 23, which shall be due __X__ immediately ___ as follows: TOTAL ASSESSMENT $700.00

IT IS FURTHER ORDERED that the defendant shall notify the United States Attorney for this district within 30 days of any change of name, residence, or mailing address until all fines, restitution, costs, and special assessments imposed by this judgment are fully paid.

Appendix D

Defendant's Soc. Sec. No.: 125-30-7222
Defendant's Date of Birth: 5-10-41

Defendant's Address:
7701 N.E. 7TH TERRACE
BOCA RATON, FLORIDA 33487

DATE: 1 MARCH 1996

26 FEBRUARY 1996
Date of Imposition of Sentence

s/ William G. Bassler
Signature of Judicial Officer

WILLIAM G. BASSLER, U.S.D.J.
Name & Title of Judicial Officer

Appendix D

IMPRISONMENT

The defendant is hereby committed to the custody of the United States Bureau of prisons to be imprisoned for a term of 240 MONTHS ON CT. 1,2,3 & 4 AND 60 MONTHS ON CT. 11,12,13,14,16,17,20,21,22 & 23 ALL TO RUN CONCURRENT TO EACH OTHER. TOTAL SENTENCE OF 240 MONTHS TO RUN CONSECUTIVE TO SENTENCE PRESENTLY SERVING.

X The court makes the following recommendations to the Bureau of Prisons: SENTENCE BE SERVED AT F.C.I. MIAMI

XX The defendant is remanded to the custody of the United States Marshal. REQUEST TO TRANSFER TO M.C.C. IN NEW YORK PENDING APPEAL.

* * *

Appendix D

SUPERVISED RELEASE

Upon release from imprisonment, the defendant shall be on supervised release for a term of 3 YEARS ON CT. 1,2,3,4,11,12,13,14,16,17,20,21,22 & 23, ALL SUCH TERMS TO RUN CONCURRENT. TOTAL SUPERVISED RELEASE IS 3 YEARS.

While on supervised release, the defendant shall not commit another federal, state, or local crime and shall not illegally possess a controlled substance. The defendant shall comply with the standard conditions that have been adopted by this court (set forth below). If this judgment imposes a restitution obligation, it shall be a conditions of supervised release that the defendant pay any such restitution that remains unpaid at the commencement of the term of supervised release. The defendant shall comply with the following additional conditions:

_X_ The defendant shall report in person to the probation office in the district to which the defendant is released within 72 hours of release from the custody of the Bureau of Prisons.

_X_ The defendant shall pay any fines that remain unpaid at the commencement of the term of supervised release.

_X_ The defendant shall not possess a firearm or destructive device.

* * *

Appendix D

STATEMENT OF REASONS

___ The court adopts the factual findings and guideline application in the presentence report.

OR

_X_ The court adopts the factual findings and guideline application in the presentence report except (see attachment, if necessary):
PARAGRAPH 190: ROLE IN THE OFFENSE +3 DEFENDANT IS MANAGER
PARAGRAPH 204: TOTAL OFFENSE LEVEL 38 RANGE OF 292-365 MONTHS

Guideline Range Determined by the Court:

Total Offense Level: 38

Criminal History Category: III

Imprisonment Range: 292 to 365 months

Supervised Release Range: 2 to 3 years

Fine Range: $25,000.00 to $250,000.00

_X_ Fine is waived or is below the guideline range, because of the defendant's inability to pay.

* * *

Appendix D

The sentence departs from the guideline range

___ upon motion of the government, as a result of defendant's substantial assistance.

_X_ for the following reasons(s): COURT FINDS THE LOSS FIGURE IN PARAGRAPH 188 IS CORRECT, HOWEVER FOR SENTENCING PURPOSES AND PURSUANT TO 5K2.0 THIS LOSS FIGURE OVER REPRESENTS THE SERIOUSNESS OF THE OFFENSE AN THE DEFENDANT WILL BE SENTENCED UTILIZING THE NJ STATE TAX LOSS OF APPROXIMATELY $14 MILLION. THIS, ALONG WITH MULTIPLE COUNT GROUPING RULES MAKE THE TOTAL OFFENSE LEVEL AT 36, CRIMINAL HISTORY AT III AND THE RANGE BECOMES 235-293.